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# Independence and ethics developments - 2009; Audit risk alerts

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A U D I T   R I S K   A L E R T

2009

# Independence and Ethics Developments

AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS

STRENGTHENING AUDIT INTEGRITY  
SAFEGUARDING FINANCIAL REPORTING



AICPA®

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AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS

2009

# Independence and Ethics Developments

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SAFEGUARDING FINANCIAL REPORTING



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Table of Contents

v

# TABLE OF CONTENTS

	<i>Paragraph</i>
Independence and Ethics Developments—2009	.01-.89
How This Alert Helps You	.01
Current Practice Environment	.02-.05
AICPA Independence and Ethics Developments	.06
New Ethics Guidance	.06
Compliance Reminder Regarding Other Authoritative Bodies	.07-.44
SEC Independence Rules	.08-.17
Recent SEC Independence Information	.18
PCAOB Rules Regarding Independence and Ethics	.19-.26
PCAOB Report on Inspections of Domestic Annually Inspected Firms	.27-.30
GAO Independence Standard	.31-.41
Internal Revenue Code	.42
Federal Deposit Insurance Corporation	.43-.44
On the Horizon	.45-.62
Proposed AICPA Ethics Interpretation	.45-.46
Other AICPA Proposals	.47-.50
AICPA PEEC Projects	.51-.60
Status of DOL Request for Comments on Independence Rules Pertaining to Employee Benefit Plan Audits	.61-.62
Resource Central	.63-.88
Publications	.63
AICPA reSOURCE: Accounting and Auditing Literature	.64
Continuing Professional Education	.65-.69
Webcasts	.70-.73
Member Service Center	.74
Hotlines	.75-.76
AICPA Governmental Audit Quality Center	.77-.79
The Center for Audit Quality	.80-.81
AICPA Employee Benefit Plan Audit Quality Center	.82-.85
Industry Web Sites	.86-.88
Appendix—Digest of the AICPA Independence Rules	.89





## How This Alert Helps You

.01 This Audit Risk Alert (alert) informs you of recent developments in the important areas of independence and ethics for accountants. This alert helps you understand your independence requirements under the AICPA Code of Professional Conduct (code) and, if applicable, certain other rule making and standard setting bodies. We present a section entitled "Digest of the AICPA Independence Rules" in plain English at the end of this alert so you can understand and apply the independence rules with greater confidence.

## Current Practice Environment

.02 Members of the accounting profession are held to very high ethical standards because they are entrusted with so much. Investors, lenders, regulators, analysts, and others place their faith and confidence in the integrity and objectivity of accountants, auditors, and other members of the profession every day.

.03 At the end of 2008, the economy was in recession, and deep-rooted troubles in our banking system and credit and real estate markets were revealed. Major institutions failed. Since then, some companies in the banking, insurance, and automobile industries have started receiving federal funds. Moving from 2008 into 2009, securities market indices worldwide dropped significantly. Later, investors began to cautiously reenter the markets amid much uncertainty about the future.

.04 Accounting professionals are at the heart of this storm. Accountants create the books and records that tell the company's financial story, and auditors issue opinions on whether the financial statements are materially correct. In good times, accounting professionals are challenged to comply with the high standards of their profession. In difficult times, incentives and pressures to maintain profits and performance increase exponentially.

.05 In times like these, accounting professionals must be aware of these pressures and be more diligent. Auditors must recognize that changing economics could sway professionals to do things that, in normal times, they would never consider doing. As always, professional skepticism is critical; practitioners also should be mindful of allotting sufficient resources to engagements so that due professional care is exercised and all services are carried out in accordance with the applicable professional standards.

## AICPA Independence and Ethics Developments

### New Ethics Guidance

#### ***Nonauthoritative Guidance Helps Members Comply With the AICPA Code***

.06 In November 2008, the Professional Ethics Executive Committee (PEEC) adopted nonauthoritative guidance titled *Guide for Complying With Rules 102–505* (guide) to help members comply with the AICPA code when no explicit interpretations or rulings apply to a member's situation. The guidance only applies to matters relating to rules in the code other than independence (for example, confidential client information or integrity and objectivity). (Note:

## 2

### Other Alerts

The AICPA code requires the use of ET section 100.01, *Conceptual Framework for AICPA Independence Standards* [AICPA, *Professional Standards*, vol. 2], when a member encounters a situation that is not addressed in the independence rules.) Under the new guide, members consider whether threats to their compliance with a rule (other than independence) in the AICPA code may be sufficiently mitigated or eliminated entirely through the application of safeguards. Members are encouraged (but not required) to apply the guidance, which is available on the AICPA's Web site at [www.aicpa.org/download/Guide\\_for\\_Complying\\_with\\_Rules\\_102\\_Through\\_505\\_11\\_10\\_08\\_Edited.pdf](http://www.aicpa.org/download/Guide_for_Complying_with_Rules_102_Through_505_11_10_08_Edited.pdf).

### Compliance Reminder Regarding Other Authoritative Bodies

.07 The independence and ethics rules under the code apply to all members of the AICPA. However, other rule making and standard setting bodies, such as the Securities and Exchange Commission (SEC), the Public Company Accounting Oversight Board (PCAOB), the Government Accountability Office (GAO), the U.S. Department of Labor (DOL), the IRS, the U.S. Department of the Treasury, banking and insurance agencies, state boards of accountancy, and state CPA societies, also have independence or other ethics rules with which members must comply, if applicable, in addition to the AICPA rules. The rules of some of these other bodies are discussed briefly in this alert. You should refer to the original text of each organization's rules for full guidance.

### SEC Independence Rules

.08 Rule 2-01, "Qualifications of Accountants," of Regulation S-X sets forth the SEC's independence rules. The rule is designed to ensure that auditors are qualified and independent of their audit clients both in fact and appearance. Accordingly, the rule establishes restrictions on financial, employment, and business relationships between an accountant and an audit client and the provisions of certain nonaudit services to an audit client.

.09 Rule 2-01(b) begins with a general standard of auditor independence, which states the following:

The Commission will not recognize an accountant as independent, with respect to an audit client, if the accountant is not, or a reasonable investor with knowledge of all relevant facts and circumstances would conclude that the accountant is not, capable of exercising objective and impartial judgment on all issues encompassed within the accountant's engagement. In determining whether an accountant is independent, the Commission will consider all relevant circumstances, including all relationships between the accountant and the audit client, and not just those relating to reports filed with the Commission.

.10 The succeeding paragraphs reflect the application of the general standard to particular circumstances. In addition, the second preliminary note to Rule 2-01 states the following:

The rule does not purport to, and the Commission could not, consider all circumstances that raise independence concerns, and these are subject to the general standard in Rule 2-01(b). In considering this standard, the Commission looks in the first instance to whether a relationship or the provision of a service: creates a mutual or conflicting

### Independence and Ethics Developments—2009

3

interest between the accountant and the audit client; places the accountant in the position of auditing his or her own work; results in the accountant acting as management or an employee of the audit client; or places the accountant in a position of being an advocate for the audit client.

.11 The rule indicates that the preceding factors are general guidance only and their application may depend on particular facts and circumstances. Thus, Rule 2-01 also provides that

... in determining whether an accountant is independent, the Commission will consider all relevant facts and circumstances. For the same reason, registrants and accountants are encouraged to consult with the Commission's Office of the Chief Accountant before entering into relationships, including relationships involving the provision of services, that are not explicitly described in the rule.

#### ***Prohibited Nonaudit Services***

.12 Practitioners are reminded that, with very limited exceptions, several nonaudit services may not be provided to audit clients and their affiliates during the audit and professional engagement period, including the following:

- Bookkeeping services (including payroll)
- Valuation, appraisal, or actuarial services
- Financial information systems design or implementation
- Human resource services
- Any service involving the performance of management functions (for example, decision making, supervisory, or ongoing monitoring functions)
- Legal services
- Expert services
- Internal audit outsourcing
- Broker-dealer, investment advisory, or investment banking services
- Certain tax services (that is, services in which a firm supports an aggressive or confidential transaction and personal tax services provided to persons in financial reporting oversight roles)

.13 Practitioners should examine all nonaudit services to be performed in light of the SEC general standard and the four guiding principles described in the preceding paragraphs .08–.11. Increased competition and pressure to maintain revenues by providing additional nonaudit services to audit clients may be intense in light of the current economic climate. Nevertheless, maintaining independence must take precedence over commercial concerns.

#### ***Initial Public Offering***

.14 If your privately held audit client files an initial public offering (IPO) with the SEC, your firm is required to be independent under the SEC's rules for all periods included in the filing (that is, the audit period). Prior to the IPO, the firm may have provided services or had business or fee relationships with the company that did not comply with the SEC independence rules. Even though the firm was not subject to SEC rules at the time the nonaudit services were

## 4

### Other Alerts

provided or the business or fee relationship existed, the firm will be held to the SEC rules for those prior audit periods. Remember, if your client intends to file an IPO and wants your firm to continue as its auditor, you must comply with SEC independence rules for all years covered by the audit opinion included in the IPO. This includes not only nonaudit services and business and fee relationships that your firm had with the client in recent years but also extends to your firm's associated entities and affiliates of your audit client (such as subsidiaries and companies under common control with your audit client).

### **Audit Partner Rotation**

.15 In 2003, the SEC adopted new audit partner rotation requirements. These rules require lead and concurring review partners on audits to rotate off the engagement team after five years of continuous service to the client. Then, the partner must remain off that engagement team for another five year period. Other partners who make decisions on significant accounting, auditing, or other reporting matters or who also have contact with the client's management and audit committee are required to rotate after seven years of continuous service to the client, at which time they must remain off the engagement for two years.

.16 The year 2009 marks the sixth year since the new rules were adopted. Therefore, unless your firm qualifies for an exemption from the rule (that is, the firm has less than 10 partners and less than 5 SEC issuer audit clients), lead and concurring review partners who have provided services to a client since 2003 should have served their final year on the engagement in 2008.

### **Communications With Audit Committees**

.17 PCAOB Rule 3526, *Communication with Audit Committees Concerning Independence* (AICPA, *PCAOB Standards and Related Rules*, Rules of the Board, "Rules"), requires auditors to communicate with the audit committee of a prospective audit client before accepting the engagement and on an annual basis. The auditor must describe in writing to the audit committee all relationships between the auditor and the client (including affiliates of both) that reasonably could be thought to bear on independence, discuss these matters with the audit committee, and document the substance of that discussion.

### **Recent SEC Independence Information**

#### ***Compilation of SEC and PCAOB Independence Rules Underway***

.18 One of the recommendations of the U.S. Treasury Department's Advisory Committee on the Auditing Profession (ACAP) was to "[p]romote the understanding of and compliance with auditor independence requirements among auditors, investors, public companies, audit committees, and boards of directors, in order to enhance investor confidence in the quality of audit processes and audits." To further understanding of and compliance with the rules, ACAP recommended that the SEC and PCAOB independence rules be compiled into a single document and posted online. According to an employee of the SEC Office of the Chief Accountant, who presented at the 2008 AICPA National Conference on Current SEC and PCAOB Developments, the compilation, which should not require rulemaking by either the SEC or the PCAOB, is underway. The compiled rules are expected sometime in 2009.

## PCAOB Rules Regarding Independence and Ethics

.19 The PCAOB has the authority to establish ethics and independence standards, in accordance with Section 103(a), "Auditing, Quality Control, and Ethics Standards," and Section 103(b), "Independence Standards and Rules," of the Sarbanes-Oxley Act of 2002 (Sarbanes-Oxley). Firms that issue audit reports on public companies are required to register with the PCAOB. Failure to do so may result in disciplinary action. Additionally, any registered public accounting firm or person associated with such a firm that fails to adhere to applicable PCAOB standards may be the subject of a PCAOB disciplinary proceeding, in accordance with Section 105, *Investigations and Disciplinary Proceedings*, of Sarbanes-Oxley. Under Section 107, *Commission Oversight of the Board*, of Sarbanes-Oxley, PCAOB rules become effective only after they are approved by the SEC. The PCAOB independence and ethics rules include the following:

- PCAOB Rule 3100, *Compliance with Auditing and Related Professional Practice Standards* (AICPA, *PCAOB Standards and Related Rules*, Rules of the Board, "Rules")
- PCAOB Rule 3500T, *Interim Ethics Standards* (AICPA, *PCAOB Standards and Related Rules*, Rules of the Board, "Rules")
- PCAOB Rule 3600T, *Interim Independence Standards* (AICPA, *PCAOB Standards and Related Rules*, Rules of the Board, "Rules")

.20 The full text of these rules can be found at [www.pcaob.org/Rules/Rules\\_of\\_the\\_Board/Section\\_3.pdf](http://www.pcaob.org/Rules/Rules_of_the_Board/Section_3.pdf).

.21 PCAOB Rule 3100 generally requires all registered public accounting firms to adhere to the PCAOB's auditing and related professional practice standards, which encompass auditing, attestation, quality control, ethics, and independence standards, in connection with the preparation or issuance of any audit report for an issuer and in their auditing and related attestation practices. This rule also requires registered public accounting firms and their associated persons to comply with all applicable standards. Accordingly, if the PCAOB's standards do not apply to an engagement or other activity of the firm, PCAOB Rule 3100, by its own terms, does not apply to that engagement or activity.

### ***Interim Ethics Standards***

.22 PCAOB Rule 3500T designates the provisions of the code on integrity and objectivity as interim ethics standards. Accordingly, in preparing or issuing an audit report, a registered public accounting firm and its associated persons should comply with ethics standards as described in Rule 102, *Integrity and Objectivity* (AICPA, *Professional Standards*, vol. 2, ET sec. 102 par. 01), and interpretations and rulings thereunder in existence as of April 16, 2003, to the extent not superseded or amended by the PCAOB.

### ***Interim Independence Standards***

.23 PCAOB Rule 3600T designates the provisions of the code regarding independence and existing standards and interpretations of the Independence Standards Board (ISB) as interim independence standards. This rule states that, in connection with the preparation or issuance of any audit report, a registered public accounting firm and its associated persons shall comply with

## 6

### Other Alerts

the following independence standards, to the extent not superseded or amended by the PCAOB:

- Rule 101, *Independence* (AICPA, *Professional Standards*, vol. 2, ET sec. 101 par. .01), and interpretations and rulings thereunder in existence on April 16, 2003
- ISB Standard No. 2, *Certain Independence Implications of Audits of Mutual Funds and Related Entities* (AICPA, *PCAOB Standards and Related Rules*, PCAOB Standards, As Amended, "Independence Standards Board")
- ISB Standard No. 3, *Employment with Audit Clients* (AICPA, *PCAOB Standards and Related Rules*, PCAOB Standards, As Amended, "Independence Standards Board")
- ISB Interpretation No. 99-1, *Impact on Auditor Independence of Assisting Clients in the Implementation of FAS 133 (Derivatives)* (AICPA, *PCAOB Standards and Related Rules*, PCAOB Standards, As Amended, "Independence Standards Board")

.24 To the extent that the SEC's rules are more or less restrictive than the PCAOB's interim independence standards, registered public accounting firms must comply with the more restrictive requirements.

### **New PCAOB Registration Requirement for Auditors of Broker-Dealers That are Nonissuers**

.25 An SEC order, which specifically exempted auditors of broker-dealers that are nonissuers from registering with the PCAOB, expired in 2009. As a result, financial statements of broker-dealers that are nonissuers for fiscal years ending after December 31, 2008, must be certified by a registered public accounting firm. In February 2009, the PCAOB staff published guidance for firms required to register that addresses, among other things, the registration process, periodic reporting, and annual fee requirements. The PCAOB does not determine, inspect for compliance with, or enforce the standards applicable to audits of entities that are nonissuers; therefore, the PCAOB's independence and ethics standards do not apply to audits of broker-dealers that are nonissuers. However, firms may voluntarily apply the PCAOB auditing standards (see [www.pcaobus.com/Standards/Staff\\_Questions\\_and\\_Answers/2004/06-30.pdf](http://www.pcaobus.com/Standards/Staff_Questions_and_Answers/2004/06-30.pdf)). Practitioners should note that the SEC independence rules applicable to registrants continue to apply to auditors of SEC-registered broker-dealers that are nonissuers. These rules do not include SEC provisions applicable to issuers (for example, partner compensation, audit partner rotation, cooling-off requirements, and communications with the audit committees about independence).

.26 The PCAOB staff questions and answers titled *Registration of Broker-Dealer Auditors* are available at [www.pcaobus.com/Registration/Staff\\_QAs\\_on\\_the\\_Registration\\_of\\_Broker-Dealers.pdf](http://www.pcaobus.com/Registration/Staff_QAs_on_the_Registration_of_Broker-Dealers.pdf).

### **PCAOB Report on Inspections of Domestic Annually Inspected Firms**

.27 In December 2008, the PCAOB issued a report titled *Report on the PCAOB's 2004, 2005, 2006, and 2007 Inspections of Domestic Annually Inspected Firms*. The report, available at [www.pcaobus.com/Inspections/Other/](http://www.pcaobus.com/Inspections/Other/)



## Independence and Ethics Developments—2009

7

2008/12-05\_Release\_2008-008.pdf, describes inspections of the eight largest domestic registered firms, which have been inspected every year since the PCAOB's inspection program began. It discusses certain issues identified in the firms' inspection reports, as well as efforts the firms made to enhance their quality control systems in light of inspection findings.

.28 The report cautions readers not to assume that all or even most of the eight firms had these issues (that is, in some cases, a deficiency may have only been noted in one firm). Rather, the report seeks to illustrate certain issues because they were believed to be significant enough to merit public discussion.

.29 One of the inspectors' overall observations was that, in some cases, it appeared that audit deficiencies may have been caused, perhaps in part, by the failure of auditors to apply an appropriate level of professional skepticism. (Note: The PCAOB is not the only organization that has made this observation. In its report addressing the audit profession as a whole, the U.S. Treasury's ACAP also raised concerns about the level of professional skepticism being exercised by auditors. In light of this, ACAP recommended that firms should "[d]evelop training materials to help foster and maintain the application of healthy professional skepticism with respect to issues of independence and other conflicts among public company auditors, and inspect auditing firms, through the PCAOB inspection process, for independence training of partners and midcareer professionals.")

.30 One area of focus in the report was the auditors' provision of nonaudit services to, and business relationships with, audit clients and their affiliates. (Note: *Affiliates* includes not only entities, such as subsidiaries, but also directors, officers, and significant shareholders of the client.) Inspectors observed a lack of formal procedures or systems to identify and monitor business relationships with audit clients and affiliates and the services being performed by these relationships. According to the report, remedies applied in these instances have included the following:

- Establishing a dedicated team to identify and evaluate business relationships in the United States and abroad
- Establishing policies and procedures for entering into business relationships
- Monitoring business relationships with audit clients and affiliates to ensure compliance with the independence rules

## GAO Independence Standard

.31 CPAs, non-CPAs, government financial auditors, and performance auditors who audit federal, state, and local governments, as well as not-for-profit and for-profit recipients of federal (and some state) grant and loan assistance, should be familiar with the ethics and independence requirements of *Government Auditing Standards* ([GAS], also referred to as the Yellow Book).

.32 The Single Audit Act of 1984 requires state and local governments and nonprofit entities to be audited under GAS if they spend a certain level of federal awards in a given fiscal year. Federal awards include federal financial assistance (such as grants, loans, loan guarantees, property, cooperative agreements, interest subsidies, insurance, food commodities, direct appropriations, or other assistance) and cost reimbursement contracts. Office of Management and Budget Circular No. A-133, *Audits of States, Local Governments, and*

## 8

### Other Alerts

*Non-Profit Organizations*, provides the guidelines and policies for performing single audits under the Single Audit Act of 1984.

**.33** Certain companies (issuers) subject to the Securities Exchange Act of 1934 may have an audit conducted in accordance with standards issued by both the PCAOB, as required by Sarbanes-Oxley, and the Comptroller General of the United States, as contained in GAS (for example, a bank that participates in federally sponsored loan programs). For such entities, auditors must satisfy both sets of standards in conducting their work.

**.34** The July 2007 Yellow Book is effective for (a) financial statement audits and attest engagements for periods beginning on or after January 1, 2008, and (b) performance audits beginning on or after January 1, 2008. The distinction between (a) and (b) is that (a) applies to the period under audit, whereas (b) applies to the engagement start date. Thus, an audit of financial statements for the period ended December 31, 2007, would be subject to the old (2003) Yellow Book, even though the audit is performed in 2008, whereas a performance audit would be subject to the new Yellow Book, regardless of the period under audit.

**.35** Chapters 2–3 of the July 2007 Yellow Book address professional ethics and independence, respectively. The GAO independence rules are in some cases very similar to the AICPA independence rules; however, in other cases (for example, rules applicable to the performance of nonaudit services), the GAO independence rules tend to be more restrictive.

**.36** To perform nonaudit services under the GAO independence rules, the auditor must observe two overarching principles: (a) firms must not provide nonaudit services that involve performing management functions or making management decisions, and (b) firms must not audit their own work or provide nonaudit services in situations in which the nonaudit services are significant or material to the subject matter of the audit.

**.37** The Yellow Book categorizes nonaudit services as follows:

- *Nonaudit services that do not impair independence and do not require compliance with the supplemental safeguards.* Examples of these services include services that are considered to be routine advice because they typically are performed in conjunction with the audit (for example, advice on the implementation of internal controls or new accounting standards).
- *Nonaudit services that would not impair independence provided the auditor complies with the supplemental safeguards.* Examples of these services include certain limited bookkeeping, IT, or human resource assistance or preparation of routine tax filings.
- *Nonaudit services that impair independence; compliance with supplemental safeguards will not overcome this impairment.* Examples of these services include posting entries to the general ledger, processing payroll that is material to the financial statements, or designing a financial reporting system. (Note: By their nature, these services violate one or both of the overarching principles discussed in the Yellow Book.)

**.38** On February 25, 2008, the Advisory Council on *Government Auditing Standards* (advisory council) met with the GAO staff in Washington, D.C., to



## Independence and Ethics Developments—2009

9

discuss a possible project to revise its independence guidance. The GAO staff sought input on the following:

- Whether the GAO independence standards should be based on a risk-based conceptual framework (instead of a traditional rules-based model)
- Whether the GAO should clarify the meaning of *personal, external, and organizational independence*
- What should be done with the frequently asked questions (FAQs)
- Independence impairments and governmental mandates

.39 To date, the staff has not initiated any new independence projects.

.40 At the time this alert was developed, plans for a November 2009 advisory council meeting, during which independence would be revisited, were being contemplated.

.41 The Yellow Book is available at [www.gao.gov/govaud/ybk01.htm](http://www.gao.gov/govaud/ybk01.htm). Valuable guidance on applying the GAO independence rules is available in the form of FAQs in *Answers to Independence Standard Questions*, which is available at [www.gao.gov/govaud/d02870g.pdf](http://www.gao.gov/govaud/d02870g.pdf).

## Internal Revenue Code

### *Disclosure or Use of Taxpayer Information*

.42 New Internal Revenue Code (IRC) regulations apply to the disclosure or use of tax return information on or after January 1, 2009. In many cases, these requirements exceed those of Rule 301, *Confidential Client Information* (AICPA, *Professional Standards*, vol. 2, ET sec. 301 par. .01). For example, information, which is broadly defined in the regulations, includes a client's name or e-mail address. Under IRC Section 7216, tax return preparers who knowingly or recklessly make unauthorized disclosures or use of information furnished to them in connection with the preparation of an income tax return are subject to criminal penalties (that is, a fine of \$1,000 or imprisonment for one year [or both] per violation). IRC Section 6713, the companion civil provision, carries similar requirements. FAQs (available on the IRS Web site at [www.irs.gov/efile/article/0,,id=188398,00.html](http://www.irs.gov/efile/article/0,,id=188398,00.html)) provide introductory information about the new regulations and links to all of the relevant authoritative information. The AICPA Tax Center provides helpful tools and resources at <http://tax.aicpa.org/Resources/Tax+Practice+Guides+and+Checklists/2008+Tax+Practice+Guides+and+Checklists/New+Section+7216+Regulations+Become+Effective.htm>.

## Federal Deposit Insurance Corporation

### *Amendments to Annual Audit and Reporting Requirements Clarify Independence and Expand Audit Committee Oversight*

.43 On June 23, 2009, the Federal Deposit Insurance Corporation's board of directors amended Part 363 of its regulations, which sets forth annual independent audit and reporting requirements for insured institutions with \$500 million or more in total assets. Among other things, the amendments clarify that auditors must comply with independence requirements of the AICPA, SEC, and PCAOB. When requirements differ, auditors should apply the most restrictive provisions. The amendments also expand the audit committee's duties with

## 10

## Other Alerts

respect to the independent auditor, making its role similar to that of audit committees governed by Sarbanes-Oxley. For example, under revised regulations, audit committees now must appoint, compensate, and oversee the independent auditor and ensure that auditor independence and other requirements of Part 363 are met (for example, audit engagement letters do not contain "unsafe and unsound" limitation of liability provisions). With certain exceptions (for example, audit committee member independence requirements and application of Part 363 at the holding company level), the new regulations become effective 30 days after they are published in the *Federal Register*.

.44 For more information, see [www.fdic.gov/news/news/financial/2009/fi09033.html](http://www.fdic.gov/news/news/financial/2009/fi09033.html).

## On the Horizon

### Proposed AICPA Ethics Interpretation

#### *Proposed Revisions to Statements on Standards for Tax Services*

.45 The AICPA Tax Executive Committee (TEC) has proposed revisions to the Statements on Standards for Tax Services (SSTSs), which are enforceable rules of conduct under Rule 201, *General Standards* (AICPA, *Professional Standards*, vol. 2, ET sec. 201 par. .01), and Rule 202, *Compliance With Standards* (AICPA, *Professional Standards*, vol. 2, ET sec. 202 par. .01), of the AICPA code. The proposed revisions to the SSTSs clarify and streamline the guidance and address changes in federal and state tax laws. Comments on the proposal were due May 15, 2009. TEC is expected to approve the final standards in August 2009.

.46 The exposure draft may be obtained at [http://tax.aicpa.org/NR/rdonlyres/F380E0EE-983D-4288-9104-1FB0415EC70C/0/FINAL\\_SSTS\\_ED\\_112608.pdf](http://tax.aicpa.org/NR/rdonlyres/F380E0EE-983D-4288-9104-1FB0415EC70C/0/FINAL_SSTS_ED_112608.pdf).

### Other AICPA Proposals

#### *Accounting and Review Services Committee*

##### *Exposure Draft to Revise Standards for Compilation and Review Engagements*

.47 The AICPA Accounting and Review Services Committee (ARSC) proposed three new Statements on Standards for Accounting and Review Services (SSARSs):

- *Framework and Objectives for Performing and Reporting on Compilation and Review Engagements*
- *Compilation of Financial Statements*
- *Review of Financial Statements*

.48 In drafting the proposed standards, the ARSC considered recommendations from the Private Company Practice Section (PCPS) Reliability Task Force. That task force comprised representatives of the ARSC, the Auditing Standards Board, the PEEC, other practitioners, academics, a banker, and a preparer of financial statements. The ARSC and PCPS believe the proposed

standards will respond to many concerns of smaller business owners, users of small business financial statements, and CPAs that serve smaller entities.

.49 Among other changes, the proposed SSARS *Review of Financial Statements* would permit a member to perform a review engagement when independence is impaired due to the performance of certain nonattest services on behalf of management to design or operate any aspect of internal control over financial reporting (described in the exposure draft as internal control services). The standard would not permit a review engagement to be performed when independence is impaired for any other reason. In addition, the proposed SSARS *Compilation of Financial Statements* would give members who are disclosing a lack of independence in their report the option of disclosing the general reason for the impairment.

.50 If approved for issuance as final SSARSs, the proposed statements would be effective for compilations and reviews of financial statements for periods beginning on or after December 15, 2010. Early application would be permitted. Comments on the proposed SSARS were due July 31, 2009. The proposed SSARS can be found at [www.aicpa.org/download/auditstd/ED\\_Reliability\\_SSARS.pdf](http://www.aicpa.org/download/auditstd/ED_Reliability_SSARS.pdf).

## AICPA PEEC Projects

### *Participation of a Covered Member's Immediate Family in an Employee Benefit Plan*

.51 In July 2009, the AICPA PEEC considered whether to propose changes to Interpretation No. 101-1, "Interpretation of Rule 101," under Rule 101 (AICPA, *Professional Standards*, vol. 2, ET sec. 101 par. .02). An exposure draft, if issued, would potentially include (a) additional guidance on how the independence rules apply to interests held through an employer's compensation or benefit plan by certain covered members' immediate family; (b) clarified guidance for covered members who were employed by or associated with an attest client; (c) technical revision to Interpretation No. 101-15, "Financial Relationships," under Rule 101 (AICPA, *Professional Standards*, vol. 2, ET sec. 101 par. .17); and (d) revisions to Ethics Ruling No. 107, "Participation in Health and Welfare Plan Sponsored by Client," of ET section 191, *Ethics Rulings on Independence, Integrity, and Objectivity* (AICPA, *Professional Standards*, vol. 2, ET sec. 191 par. .214–.215). For pending and completed exposure drafts, see [www.aicpa.org/Professional+Resources/Professional+Ethics+Code+of+Professional+Conduct/Professional+Ethics/Exposure+Drafts+-+Standard+Setting/](http://www.aicpa.org/Professional+Resources/Professional+Ethics+Code+of+Professional+Conduct/Professional+Ethics/Exposure+Drafts+-+Standard+Setting/).

### *Affiliate Task Force*

.52 A PEEC task force is identifying and evaluating the rules of the various standard setters that address the independence implications of an interest in or relationship with an affiliate of an attest client. Once the task force identifies all the relevant standards, it plans to analyze the information and provide recommendations to the PEEC about whether to address any perceived gaps in the AICPA literature.

### *Inadvertent Violations of the Code*

.53 A PEEC task force is considering whether the AICPA code should, under certain circumstances, provide relief to members when they inadvertently violate a rule in the code. Among other things, the task force has

## 12

### Other Alerts

considered what would constitute an inadvertent violation, when matters should be brought to an audit committee's attention, and how such a provision would apply to violations of Interpretation No. 101-3, "Performance of Nonattest Services," under Rule 101 (AICPA, *Professional Standards*, vol. 2, ET sec. 101 par. .05).

### ***eXtensible Business Reporting Language and International Financial Reporting Standards Task Forces***

.54 Two PEEC task forces are considering whether to revise Interpretation No. 101-3 for two types of nonattest services that are expected to become more prevalent in the next several years: assisting clients with their adoption of eXtensible Business Reporting Language and transitioning financial reporting from U.S. generally accepted accounting principles (GAAP) to International Financial Reporting Standards. Among other things, certain generic activities (for example, training and assisting clients in managing implementation efforts) are being considered by the task forces.

### ***Confidential Client Information***

.55 A PEEC task force is considering whether a member would violate Rule 301 if he or she provided client information, such as statistical information or other data, to a third party without the client's consent if the information does not identify the client. In the fact pattern being examined, the third party would use the information for research or benchmarking purposes.

### ***International Ethics Convergence and Monitoring***

.56 The visibility of the International Federation of Accountants (IFAC) *Code of Ethics for Professional Accountants* (code) in the United States has grown in recent years as business has become increasingly global, and the AICPA has begun the process of converging its code with the IFAC guidance. Consequently, CPA firms of all sizes are being asked to confirm their compliance with global standards.

.57 The following scenarios illustrate these points:

- A three partner firm in Albany, New York, is the auditor for a beverage manufacturer. In a major acquisition, a Canadian company purchases the manufacturer. The new parent's auditor asks the U.S. firm to confirm that it is independent of the new owner under international standards.
- A local firm is part of a global accounting association that is deemed, under international standards, to be a network. All firms in the network must be independent of the other firms' audit and review clients, in accordance with those standards. In fact, the network requires its members to meet global ethics standards for all multinational assurance engagements.
- A regional firm in southern California serves as auditor of a small Los Angeles-based software developer that acquires a company in Bangalore, India. The Indian company's significant vendors and its lenders expect to rely on the California firm's audit report and, thus, expect the firm to meet global standards.
- A small firm's client expands its business by opening a branch office in China. Lessors, vendors, and lenders in China ask the

firm to audit the client's financial information in accordance with international auditing standards, which will call for the firm to comply with international ethics standards.

.58 In April 2009, the International Ethics Standards Board for Accountants (IESBA) adopted revisions to the IFAC code, which clarify the language of the IFAC code (for example, the use of *should* versus *must*) and enhance the overall language of the IFAC code. Included in those revisions were substantive revisions to Section 290, *Independence—Audit and Review Engagements*, which addressed internal audit services, the impact of significant fees to an accounting firm, and contingent fees. With certain exceptions, the new IFAC code will become effective on January 1, 2011, with earlier adoption permitted. For example, rules applicable to audits of public interest entities become effective January 1, 2012, and transition allowances have been incorporated into the rules for auditor rotation and certain nonassurance services. The revised IFAC code can be found in the updated agenda papers at [www.ifac.org/Ethics/Meeting-Resource.php?MID=0184&type=Updated+Agenda](http://www.ifac.org/Ethics/Meeting-Resource.php?MID=0184&type=Updated+Agenda).

.59 The IESBA has declared that it will not put forth any more proposals for a period of at least two years. This "quiet period" will allow member bodies (such as the AICPA) time to align their national codes with the new IFAC code.

### **Three Year Project Agenda**

.60 The AICPA Professional Ethics Division maintains a three year project agenda on its Web site that lists all current and future PEEC projects. The agenda can be found at [www.aicpa.org/download/ethics/PEEC\\_Project\\_Agenda.pdf](http://www.aicpa.org/download/ethics/PEEC_Project_Agenda.pdf).

### **Status of DOL Request for Comments on Independence Rules Pertaining to Employee Benefit Plan Audits**

.61 On September 11, 2006, the DOL issued a request for information (RFI) seeking public comment on the advisability of the DOL amending the auditor independence rules for employee benefit plan audits subject to the Employee Retirement Income Security Act of 1974 (ERISA). This is the first time the DOL has considered its independence requirements since DOL Interpretive Bulletin 75-9 (29 U.S. *Code of Federal Regulations* (CFR) 2509.75-9), *Interpretive bulleting relating to guidelines on independence of accountant retained by Employee Benefit Plan*, was issued in 1975. The DOL RFI notes that the current DOL requirements conflict with AICPA and SEC independence requirements and have caused confusion among practitioners. The comment period closed on December 11, 2006. To date, the DOL has not issued a response to the feedback it received regarding its RFI.

.62 The DOL's RFI can be found at [http://ebpaqc.aicpa.org/NR/rdonlyres/7EA13B14-C1AE-42EF-9FD1-B1B1353A962F/0/DOL\\_Auditor\\_Independence\\_RFI.pdf](http://ebpaqc.aicpa.org/NR/rdonlyres/7EA13B14-C1AE-42EF-9FD1-B1B1353A962F/0/DOL_Auditor_Independence_RFI.pdf). The comment letters received by the DOL can be found at [www.dol.gov/ebsa/regs/cmt-IndPlanAccountants.html](http://www.dol.gov/ebsa/regs/cmt-IndPlanAccountants.html).

## **Resource Central**

### **Publications**

.63 Practitioners may find the following publications useful when considering independence and ethics issues:

## 14

### Other Alerts

- *Independence Compliance: Checklists and Tools for Complying With AICPA and GAO Independence Requirements* (product no. 006661kk)
- *Independence Compliance: Checklists and Tools for Complying With AICPA, SEC, and PCAOB Independence Requirements* (product no. 006660kk)

### AICPA reSOURCE: Accounting and Auditing Literature

.64 The AICPA has created your core accounting and auditing library online. AICPA reSOURCE is now customizable to suit your preferences or your firm's needs. Or, you can sign up for access to the entire library. Get access—anytime, anywhere—to the AICPA's latest *Professional Standards*, *Technical Practice Aids*, *Audit and Accounting Guides*, *Audit Risk Alerts*, *Accounting Trends & Techniques*, and more. To subscribe to this essential online service for accounting professionals, go to [www.cpa2biz.com](http://www.cpa2biz.com).

### Continuing Professional Education

.65 The AICPA offers a number of continuing professional education (CPE) courses on ethics and independence that are valuable to CPAs working in public practice and industry, including the following:

- *Ethics for Tax Practice Professionals: Circular 230 and the SSTs* (product no. 738702HSkk [CD-ROM], 158700kk [online])
- *Ethics: Non-Attest Services, Integrity and Objectivity* (product no. 739416HSkk [CD-ROM], 159413kk [online])
- *Independence* (product no. 739179HSkk [CD-ROM], 159179kk [online])
- *Selected Topics in Professional Ethics* (product no. 738384HSkk [CD-ROM], 158384kk [online])
- *Professional Ethics: 2009/2010 Update* (product no. 739431HSkk [CD-ROM], 159431kk [online])
- *Professional Ethics: AICPA's Comprehensive Course* (product no. 738393HSkk [CD-ROM], 732312kk [text])
- *Professional Ethics: Complying With the GAO Rules* (product no. 739440HSkk [CD-ROM], 159440kk [online])
- *Professional Ethics: Complying With SEC and PCAOB Rules* (product no. 739470HSkk [CD-ROM], 159470kk [online])
- *Professional Ethics for CPAs in Business & Industry* (product no. 738900HSkk [CD-ROM], 158900kk [online])
- *Professional Ethics: Navigating the Gray Areas* (product no. 739450HSkk [CD-ROM], 159450kk [online])
- *Real World Business Ethics for CPAs in A&A: How Will You React?* (product no. 733602kk [text])
- *Real World Business Ethics for CPAs in Business & Industry: How Will You React?* (product no. 733592kk [text])
- *Real World Business Ethics: How Would You React?* (product no. 731686kk [text])
- *Real Word Business Ethics for Tax Practitioners: How Will You React?* (product no. 733612kk [text])



.66 The AICPA interactive CD-ROM course on independence titled *Independence* teaches, among other things, the AICPA, SEC, PCAOB, and GAO independence rules and qualifies for eight hours of CPE credits. See [www.cpa2biz.com/AST/Main/CPA2BIZ\\_Primary/Ethics/PRDOVR~PC-739155HS/PC-739155HS.jsp](http://www.cpa2biz.com/AST/Main/CPA2BIZ_Primary/Ethics/PRDOVR~PC-739155HS/PC-739155HS.jsp).

.67 Visit [www.cpa2biz.com](http://www.cpa2biz.com) for a complete list of CPE courses.

### Online CPE

.68 AICPA CPEExpress, offered exclusively through CPA2Biz, is the AICPA's flagship online learning product. AICPA members pay \$180 for a new subscription and \$149 for the annual renewal. Nonmembers pay \$435 for a new subscription and \$375 for the annual renewal. Divided into 1-credit and 2-credit courses that are available 24 hours a day, 7 days a week, AICPA CPEExpress offers hundreds of hours of learning in a wide variety of topics. Some courses that address ethics and independence issues include the following:

- 2008 Annual A&A Update—On the Horizon—Issues for Audits of Public Entities
- 2008 Annual A&A Update—Various Issues Affecting Auditors
- 2008 Public Company Update: SEC Guidance
- Compilations and Reviews: Independence Considerations
- Comp & Review Engagements: Recent SSARS Developments and Current Practice Issues
- Current SEC and PCAOB Developments during Q3 '08
- Ethics: AA&C LLP—Accounting Firm Practice Development Committee
- Ethics: BAN&K Advisory Services LLC—You Are the Audit Partner
- Ethics: Department of Enforcement—You Are the Accounting Investigator
- Ethics: Forensic Review Services LLC—You Are the Forensic Auditor
- Ethics: Incisive Lasers Corporation—You Are the Outside Counselor
- Ethics: Megatron Corp.—You Are the Corporate Controller
- Ethics: Military Communications Corp.—You Are the Outside Tax Advisor
- Ethics: Pointer Electronics, Inc.—You Are the Audit Partner
- Ethics: Precious Mining Inc.—You Are the Audit Committee Chair
- Ethics: Radar One, LLP—You Are the Amended Return Preparer
- Ethics: Scrap Metal Aggregators, Inc.—You Are the Tax Return Preparer
- Ethics: Superlative Software, Corp.—You Are the CFO
- In a CPA's Professionalism We Must Trust
- Single Audit & Yellow Book Deficiencies: Independence, Single or Prog Audit, A-133 Major Prog Audit

## 16

### Other Alerts

- Small Business Auditing: Independence Considerations
- Yellow Book: Ethical Principles and General Standards

.69 To register or learn more, visit [www.cpa2biz.com](http://www.cpa2biz.com).

### Webcasts

.70 Stay plugged in to what is happening and earn CPE credit right from your desktop. AICPA webcasts are high quality, two-hour CPE programs that bring you the latest topics from the profession's leading experts. Broadcast live, they allow you to interact with the presenters and join in the discussion. If you cannot make the live event, each webcast is archived and available on CD-ROM.

#### *CFO Quarterly Roundtable Series*

.71 The CFO Quarterly Roundtable Series, brought to you each calendar quarter via webcast, covers a broad array of "hot topics" that successful organizations employ and subjects that are important to the CFO's personal success. From financial reporting, budgeting, and forecasting to asset management and operations, the roundtable helps CFOs, treasurers, controllers, and other financial executives excel in their demanding roles.

#### *SEC Quarterly Update Series*

.72 The SEC Quarterly Update Webcast Series, brought to you each calendar quarter, showcases the profession's leading experts on what is "hot" at the SEC. From corporate accounting reform legislation and new regulatory initiatives to accounting and reporting requirements and corporate finance activities, these hard-hitting sessions will keep you "plugged in" to what is important. A must for preparers in public companies and practitioners who have public company clients, this is the place to be when it comes to knowing about the areas of current interest at the SEC.

#### *IFRS Quarterly Webcast Series*

.73 The International Financial Reporting Standards (IFRS) Quarterly Webcast Series, brought to you each calendar quarter, is part of a multistep educational process to get practitioners, financial managers, and auditors up to speed on all aspects of IFRS implementation. Over the course of the quarterly series, IFRS standards will be covered in depth. International harmonization is quickly approaching, and this series will help both accountants and auditors stay abreast of the developments and changes they will need to implement.

### Member Service Center

.74 To order AICPA products, receive information about AICPA activities, and get help with your membership questions, call the AICPA Service Operations Center at (888) 777-7077.

### Hotlines

#### *Ethics Hotline*

.75 The AICPA offers an Ethics Hotline. Members of the AICPA's Professional Ethics Team answer inquiries concerning independence and other behavioral issues related to the application of the AICPA code. You can reach the Ethics Hotline at (888) 777-7077 or by e-mail at [ethics@aicpa.org](mailto:ethics@aicpa.org).



### ***Accounting and Auditing Technical Hotline***

**.76** Do you have a complex technical question about GAAP, other comprehensive bases of accounting, or other technical matters? If so, use the AICPA's Accounting and Auditing Technical Hotline. AICPA staff will research your question and call you back with the answer. The hotline is available from 9 a.m. to 8 p.m. EST on weekdays. You can reach the Technical Hotline at (877) 242-7212 or online at [www.aicpa.org/Professional+Resources/Accounting+and+Auditing/Accounting+and+Auditing+Technical+Help/](http://www.aicpa.org/Professional+Resources/Accounting+and+Auditing/Accounting+and+Auditing+Technical+Help/).

### **AICPA Governmental Audit Quality Center**

**.77** The Governmental Audit Quality Center (GAQC) is a firm-based, voluntary membership center designed to help CPAs meet the challenges of performing quality audits in this unique and complex area. The GAQC's primary purpose is to promote the importance of quality governmental audits and the value of such audits to purchasers of governmental audit services. The GAQC also offers resources to enhance the quality of a firm's governmental audits.

**.78** The mission of the GAQC is to do the following:

- Raise awareness about the importance of governmental audits
- Serve as a comprehensive resource provider on governmental audits for member firms
- Create a community of firms that demonstrates a commitment to governmental audit quality
- Provide center members with an online forum tool for sharing best practices and discussing audit, accounting, and regulatory issues
- List member firms to enable purchasers of governmental audit services to identify firms that are members
- Provide information about the center's activities to other governmental audit stakeholders

**.79** For more information about the GAQC visit <http://gaqc.aicpa.org>.

### **The Center for Audit Quality**

**.80** The Center for Audit Quality (CAQ), which is affiliated with the AICPA, was created to serve investors, public company auditors, and the markets. The CAQ's mission is to foster confidence in the audit process and aid investors and the capital markets by advancing constructive suggestions for change rooted in the profession's core values of integrity, objectivity, honesty, and trust.

**.81** To accomplish this mission, the CAQ works to make public company audits even more reliable and relevant for investors in a time of growing financial complexity and market globalization. The CAQ also undertakes research, offers recommendations to enhance investor confidence and the vitality of the capital markets, issues technical support for public company auditing professionals, and helps facilitate the public discussion about modernizing business reporting. The CAQ is a voluntary membership center that provides education, communication, representation, and other means to member firms that audit or are interested in auditing public companies. To learn more about the CAQ, visit <http://thecaq.aicpa.org>.

### **AICPA Employee Benefit Plan Audit Quality Center**

.82 The AICPA Employee Benefit Plan Audit Quality Center (EBPAQC) is a firm-based, voluntary membership organization for firms that perform or are interested in performing ERISA employee benefit plan audits. The EBPAQC was established to promote the quality of employee benefit plan audits.

.83 To achieve this goal, the EBPAQC has created a community of firms that demonstrate a commitment to employee benefit audit quality, and it supports those firms by doing the following:

- Providing members with timely communication of regulatory developments, best practices guidance, and technical updates
- Providing members with an online community forum for sharing best practices, as well as discussions on audit, accounting, and regulatory issues
- Maintaining relationships with, and acting as a liaison to, the DOL on behalf of member firms
- Providing center members with a marketing toolkit to facilitate promotion of their membership in the center
- Providing information about the center's activities to other employee benefit plan stakeholders

.84 The increasing complexity of employee benefit plan auditing and increased scrutiny by the DOL have resulted in a significant number of changes and issues for auditing firms and CPAs in general. Firms and CPAs will benefit from the assistance of the center as a resource for improving employee benefit plan audit quality.

.85 For more information about the EBPAQC, visit <http://ebpaqc.aicpa.org>.

### **Industry Web Sites**

.86 The Internet covers a vast amount of information that may be valuable to auditors, including current industry trends and developments. Some of the more relevant sites for auditors include those shown in the following table:

## Independence and Ethics Developments—2009

19

<b>Web Site Name</b>	<b>Content</b>	<b>Web Site</b>
AICPA	Summaries of recent auditing and other professional standards, as well as other AICPA activities	<a href="http://www.aicpa.org">www.aicpa.org</a> <a href="http://www.cpa2biz.com">www.cpa2biz.com</a> <a href="http://www.ifrs.com">www.ifrs.com</a>
AICPA Professional Ethics Executive Committee (PEEC)	AICPA Code of Professional Conduct; PEEC standards setting projects and meeting information; information on the ethics enforcement process, including discipline actions; as well as an array of other resources	<a href="http://www.aicpa.org/Professional+Resources/Professional+Ethics+Code+of+Professional+Conduct/">www.aicpa.org/Professional+Resources/Professional+Ethics+Code+of+Professional+Conduct/</a>
Board of Governors of the Federal Reserve System (FRB)	Advisory dated 2006 regarding the use of limitation of liability provisions in engagement letters with public and nonpublic financial institutions	<a href="http://www.federalreserve.gov/boarddocs/srletters/2006/SR0604a1.pdf">www.federalreserve.gov/boarddocs/srletters/2006/SR0604a1.pdf</a>
Department of Labor (DOL)	DOL Regulation 2509.75-9, <i>Interpretive bulletin relating to guidelines on independence of accountant retained by Employee Benefit Plan</i> , and contact information	<a href="http://www.dol.gov/">www.dol.gov/</a>
Government Accountability Office (GAO)	<i>Government Auditing Standards</i> independence standard, frequently asked questions on independence, slide presentation on independence, and contact information	<a href="http://www.gao.gov/govaud/ybk01.htm/">www.gao.gov/govaud/ybk01.htm/</a>
Federal Deposit Insurance Corporation (FDIC)	FDIC regulations (12 U.S. <i>Code of Federal Regulations</i> [CFR] Part 363), <i>Annual Independent Audits and Reporting Requirements</i>	<a href="http://www.fdic.gov/regulations/laws/rules/2000-8500.html#2000part363">www.fdic.gov/regulations/laws/rules/2000-8500.html#2000part363</a>

(continued)

## 20

### Other Alerts

<b>Web Site Name</b>	<b>Content</b>	<b>Web Site</b>
International Federation of Accountants (IFAC)	Pronouncements, projects, and key contacts of the International Ethics Standards Board for Accountants (IESBA), including the IESBA's <i>Code of Ethics for Professional Accountants</i>	<a href="http://www.ifac.org/Ethics/">www.ifac.org/Ethics/</a>
Public Company Accounting Oversight Board (PCAOB)	Information on accounting and auditing activities of the PCAOB, including those on independence	<a href="http://www.pcaob.org">www.pcaob.org</a>
Securities and Exchange Commission (SEC)	Information from the Office of the Chief Accountant for accountants and auditors, including independence; current SEC rulemaking; final rule releases 33-8183A and 33-8183, <i>Strengthening the Commission's Requirements Regarding Auditor Independence</i> ; and key contact information	<a href="http://www.sec.gov">www.sec.gov</a>

\* \* \* \*

**.87** This Audit Risk Alert replaces *Independence and Ethics Developments—2008*.

**.88** The Audit Risk Alert *Independence and Ethics Developments* is published annually. As you encounter audit or industry issues that you believe warrant discussion in next year's Audit Risk Alert, please feel free to share them with us. Any other comments that you have about the Audit Risk Alert also would be appreciated. You may e-mail these comments to [dridge@aicpa.org](mailto:dridge@aicpa.org) or write to

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Durham, NC 27707-8110

## Appendix—Digest of the AICPA Independence Rules

A plain-English description of the AICPA independence rules follows. The purpose of this section is to help you to understand independence requirements under the AICPA Code of Professional Conduct (code) and, if applicable, other rule making and standard setting bodies. *Independence* generally implies one's ability to act with integrity and exercise objectivity and professional skepticism. The AICPA and other rule making bodies have developed rules that establish and interpret independence requirements for the accounting profession. We use the term *rules* broadly to also mean standards, interpretations, rulings, laws, regulations, opinions, policies, or positions. This guide discusses in plain English the independence requirements of the principal rule making bodies in the United States so you can understand and apply them with greater confidence and ease.

This section of the alert is intentionally concise, so it does not cover all the rules (some of which are complex), nor does it cover every aspect of the rules herein. Nonetheless, this guide should help you identify independence issues that may require further consideration. Therefore, you should always refer directly to the rules, in addition to your firm's policies on independence, for complete information.

### Conventions and Key Terms Used

The following are some of the conventions used in this section of the alert:

- The word ***Note*** in boldface italics emphasizes important points, highlights applicable government regulations, or indicates that a rule change may soon occur.
- AICPA interpretations and rulings to the code are linked.
- Web addresses (universal resource locators or URLs) and hyperlinks to other sources of information are provided.
- Information on additional resources appears at the end of this section to help you resolve your independence issues (see the question "Where Can I Find Further Assistance With My Independence Questions?")

We describe the rules of the Securities and Exchange Commission (SEC) and Public Company Accounting Oversight Board (PCAOB)—that is, those that apply to audits of SEC registrants and issuers—in boxed text (like this one) and provide citations to specific rules. Generally, we provide these descriptions when the SEC and PCAOB either impose additional requirements or their rules otherwise differ from the AICPA rules.

This section uses the following key terms:

**Client (or attest client).** An entity with respect to which independence is required.

**Firm.** A form of organization permitted by law or regulation (whose characteristics conform to resolutions of the AICPA council) that is engaged in the practice of public accounting.

**SEC registrant.** An issuer filing an initial public offering, a registrant filing periodic reports under the securities laws, a sponsor or manager of an investment fund, or a foreign private issuer that is or is in the process of becoming an SEC registrant. In this appendix, *SEC audit client* means an SEC registrant and its affiliates, as defined in the SEC rules.

**Issuer.** An entity whose securities are registered under the securities laws or that is required to file reports under Section 10(A) of the Securities Exchange Act of 1934 or that files or has filed a registration statement that has not yet become effective under the Securities Act of 1933.

**Note:** Certain SEC registrants (for example, broker-dealers and hedge funds) are not issuers (that is, they are nonissuers). These entities' auditors will not be subject to the PCAOB independence rules and will be exempt from certain SEC independence rules.

## What Is Independence?

*Independence* is defined in ET section 100.01, *Conceptual Framework for AICPA Independence Standards* (AICPA, *Professional Standards*, vol. 2), and is referred to herein as *the conceptual framework*, as follows:

**Independence of mind.** The state of mind that permits the performance of an attest service without being affected by influences that compromise professional judgment, thereby allowing an individual to act with integrity and exercise objectivity and professional skepticism.

**Independence in appearance.** The avoidance of circumstances that would cause a reasonable and informed third party, having knowledge of all relevant information, including safeguards applied, to reasonably conclude that the integrity, objectivity, or professional skepticism of a firm or a member of the attest engagement team had been compromised.

These definitions reflect the long-standing professional requirement that members who provide services to entities for which independence is required be independent both "in fact" (that is, "of mind") and in appearance.

## What Should I Do if No Specific Guidance Exists on My Particular Independence Issue?

The "Other Considerations" section of Interpretation No. 101-1 "Interpretation of Rule 101," under Rule 101, *Independence* (AICPA, *Professional Standards*, vol. 2, ET sec. 101 par. .02), recognizes that it is impossible for the code to identify all circumstances in which the appearance of independence might be questioned.

Specifically, Interpretation No. 101-1 requires that members use the risk-based approach described in the conceptual framework when making independence decisions involving matters that are not specifically addressed in the independence interpretations and rulings in the code. When threats to independence are not at an acceptable level, safeguards must be applied to eliminate the threats or reduce them to an acceptable level. In cases when threats to independence are not at an acceptable level, and thereby require the application of safeguards, the threats identified and the safeguards applied to eliminate the threats or reduce them to an acceptable level must be documented.

The conceptual framework provides a valuable tool to help you comply with the requirement in the "Other Considerations" section to evaluate whether a specific circumstance that is not addressed in the code would pose an unacceptable threat to your independence.

### When Is Independence Required, and Who Sets the Rules?

AICPA *Professional Standards* require your firm, including the firm's partners and professional employees, to be independent in accordance with Rule 101 of the code whenever your firm performs an attest service for a client. Attest services include the following:

- Financial statement audits
- Financial statement reviews
- Other attest services as defined in the Statements on Standards for Attestation Engagements

Performing a compilation of a client's financial statements does not require independence. However, if a nonindependent firm issues such a compilation report, the report must state, "I am (we are) not independent with respect to XYZ Company."<sup>1</sup>

You and your firm are not required to be independent to perform services that are not attest services (for example, tax preparation or advice or consulting services, such as personal financial planning) if they are the only services your firm provides to a particular client.

**Note:** You should familiarize yourself with your firm's independence policies, quality control systems, and list or database of attest clients.

### In Addition to the AICPA, Who Else Sets Independence Rules?

Many clients are subject to oversight and regulation by governmental agencies. For example, the Government Accountability Office (GAO) sets independence rules that apply to entities audited under *Government Auditing Standards* (also referred to as the Yellow Book). For these clients (and others, such as those subject to regulation by the SEC or Department of Labor [DOL]), you and your firm also must comply with the independence rules established by those agencies.

The SEC regulates SEC registrants and issuers and establishes the qualifications of independent auditors. This section refers to these independence rules as *SEC rules*.

The PCAOB, a private standards setting body whose activities are overseen by the SEC, is authorized to set, among other things, auditing, attestation, quality control, ethics, and independence standards for accounting firms that audit issuers. The PCAOB adopted interim ethics standards based on the following provisions of the code: Rule 102, *Integrity and Objectivity* (AICPA, *Professional Standards*, vol. 2, ET sec. 102 par. .01); Rule 101; and interpretations and rulings under those rules as of April 16, 2003. It also adopted Independence Standards Board (ISB) standards. To the extent that the SEC's rules are more or less restrictive than the PCAOB's interim independence standards, registered public accounting firms must comply with the more restrictive requirements.

<sup>1</sup> See paragraph .19 of AR section 100, *Compilation and Review of Financial Statements* (AICPA, *Professional Standards*, vol. 2).

## 24

### Other Alerts

In addition to its detailed rules, the SEC looks to its general standard of independence and four basic principles to determine whether independence is impaired. The general standard is an appearance standard that considers whether a reasonable investor with knowledge of all relevant facts and circumstances would conclude that an accountant is independent.

Under the four basic principles, an auditor cannot (1) function in the role of management, (2) audit his or her own work, (3) serve in an advocacy role for the client, or (4) have a mutual or conflicting role with the client.

Other organizations that establish independence requirements that may be applicable to you and your firm include the following:

- State boards of accountancy
- State CPA societies
- Federal and state agencies

You should contact these organizations directly for further information.

**Note:** Generally, the AICPA independence rules will apply to you in all situations involving an attest client. If an additional set of rules governing an engagement also applies, you should comply with the most restrictive rule or the most restrictive portions of each rule.

Once you determine that your firm provides attest services to a client and which rules apply, the next step is to determine how the rules apply to you.

### Applying the Rules—Covered Members and Other Firm Professionals

#### *How Do the Independence Rules Apply to Me?*

Whenever you are a covered member, you become subject to the full range of independence rules with regard to a specific client. You are a covered member if you are any of the following:

1. An individual on the client's attest engagement team
2. An individual in a position to influence the client's attest engagement
3. A partner or manager who provides more than 10 hours of nonattest services to the attest client
4. A partner in the office in which the lead attest engagement partner primarily practices in connection with the client's attest engagement
5. The firm, including the firm's employee benefit plans
6. An entity whose operating, financial, or accounting policies can be controlled<sup>2</sup> by any of the individuals or entities described in items 1–5 or by two or more such individuals or entities if they act together

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<sup>2</sup> As defined by generally accepted accounting principles for consolidation purposes.



The SEC uses the term *covered person*<sup>3</sup> to describe the individuals in a firm who are subject to SEC independence rules. This term is largely consistent with the AICPA's term *covered member*. The only difference between the two definitions is that of classification. The AICPA considers consultants to be in a position to influence the engagement (the SEC uses the term *chain of command*), whereas the SEC considers these persons to be on the attest engagement team. Overall, the definitions are the same.

**Note:** This alert uses the term *covered member* (and *covered person* with respect to SEC rules) extensively in explaining the "personal" independence rules (for example, rules that apply to you and your family's loans, investments, and employment). Therefore, it is important that you understand these terms before proceeding. Also, remember to check your firm's policies to determine whether they are more restrictive than the AICPA or SEC rules.

### ***Do Any of the Rules Apply to Me if I Am Not a Covered Member?***

Yes, these rules apply in certain circumstances, even if you are not a covered member. Due to their magnitude, two categories of relationships impair independence even if you are not a covered member. These relationships are defined as follows:

- Director, officer, or employee (or in any capacity equivalent to a member of management) of the client, promoter, underwriter, voting trustee, or trustee of any of the client's employee benefit plans
- Owner of more than 5 percent of an attest client's outstanding equity securities (or other ownership interests)

The independence rules prohibit these relationships if you are a partner or professional employee in a public accounting firm.

### ***What if I Was Formerly Employed by a Client, or I Was a Member of the Client's Board of Directors?***

You must be aware of a number of things, including the following:

- You may not participate in the client's attest engagement, or be in a position to influence the engagement, for any periods covering the time that you were associated with the client. So, for example, if you worked for the client in 2008, you would be prohibited from serving on the client's audit engagement for the fiscal year 2008 financial statements. You also could not serve in a position that would allow you to influence the fiscal 2008 engagement (for example, you could not directly or indirectly supervise the audit engagement partner).
- Before becoming a covered member, you must do the following:

<sup>3</sup> See Rule 2-01(f)(11). Also, see "Covered Persons in the Firm," in the SEC's final rule release [Section IV (H)(9)].

## 26

### Other Alerts

- Terminate any relationships with the client as described in Interpretation No. 101-1<sup>4</sup>
- Dispose of all financial interests in the client<sup>5</sup>
- Collect and repay all loans to or from the client (except those specifically permitted or grandfathered)<sup>6</sup>
- Cease active participation in the client's employee benefit plans (except for benefits under the Consolidated Omnibus Budget Reconciliation Act of 1985)
- Liquidate or transfer any vested benefits in the client's retirement plans

#### ***What Rules Apply if I Am Considering Employment With an Attest Client?***

If an attest client offers you employment or you seek employment with an attest client, you may need to take certain actions. If you are on that client's attest engagement team or can otherwise influence the engagement, you must promptly report any employment negotiations with the client to the appropriate person in your firm. You cannot participate in the engagement until your negotiations with the client end.

#### ***What if I Accept Employment or a Board Position With an Attest Client?***

Being employed by a client or a member of the client's board of directors impairs independence. However, even if you leave your firm to take a position with a client, independence still may be affected. This would be the case if you accept a key position with the client, which means that you prepare financial statements or accounting records or are otherwise able to influence the client's statements or records. A few examples of key positions are controller, CFO, or treasurer. Remember that the substance, and not only the position title, determines whether a position is considered "key."

If you meet the following conditions, having a key position with a client will not impair your firm's independence:

- The amounts that the firm owes you (capital balance or retirement benefits) are based on a fixed formula and are not material to the firm.
- You cannot influence the firm's operations or financial policies.
- You do not participate or appear to participate in the firm's business or professional activities.

Your firm must consider whether it should apply additional procedures to ensure that your transition to the client has not compromised the firm's

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<sup>4</sup> This includes the director, officer, employee, or in any capacity equivalent to that of a member of management, promoter, underwriter, or voting trustee, or trustee for the entity's pension and profit-sharing trust.

<sup>5</sup> See the "When Do My (or My Family's) Financial Interests Impair Independence?" section in this alert.

<sup>6</sup> Also see Interpretation No. 101-5, "Loans From Financial Institution Clients and Related Terminology," under Rule 101, *Independence* (AICPA, *Professional Standards*, vol. 2, ET sec. 101 par. .07).

## Independence and Ethics Developments—2009

27

independence and that independence will be maintained going forward. Some things the firm should consider are the following:

- Whether you served on the engagement team and for how long
- Positions you held with the firm and your status
- Your position and status with the client
- The amount of time that has passed since you left the firm

Based on these factors, the firm may decide to do the following:

- Adjust the audit plan to reduce the risk that your knowledge of the plan could lessen the audit's effectiveness
- Reconsider the successor engagement team to ensure it has sufficient stature and experience to deal effectively with you in your new position
- Perform an internal technical review of the next attest engagement to determine whether engagement personnel exercised the appropriate level of professional skepticism in evaluating your work and representations<sup>7</sup>

Under SEC rules, if a former partner will be in an accounting role or financial reporting oversight role with an SEC audit client, he or she may not have the following:

- A capital balance with the firm
- A financial arrangement with the firm (for example, retirement benefits) that is not fully funded by the firm
- Influence over the firm's operations or financial policies

The SEC uses the terms *accounting role* and *financial reporting oversight role*<sup>8</sup> in its rules; taken together, these terms are consistent with the AICPA term *key position*. The SEC also requires a one year cooling-off period for members of the audit engagement team of an issuer who assume a financial reporting oversight role with the client. In other words, if an engagement team member who participated on the audit of the current (or immediately preceding) fiscal year goes to work for a client, the firm's independence would be impaired.

Only members who provided fewer than 10 hours of audit, review, or other attest services to the client (and did not serve as either the lead or concurring partner for the client) would be excluded from the audit engagement team for purposes of this rule.

This rule applies to an issuer and its consolidated entities.

<sup>7</sup> An objective professional with the appropriate stature and expertise should perform this review and the firm should take any recommendation(s) that result from the review.

<sup>8</sup> *Accounting role or financial reporting role* means a role in which a person is in a position to or does (1) exercise more than minimal influence over the contents of the accounting records or anyone who prepares them or (2) exercise influence over the contents of the financial statements or anyone who prepares them, such as when the person is a member of a board of directors or similar management or governing body, CEO, president, CFO, general counsel, chief accounting officer, controller, director of internal audit, director of financial reporting, treasurer, vice president of marketing, or any equivalent position.

## Applying the Rules—Family Members

### *When Is My Family Subject to the Rules?*

If you are a covered member with respect to a client, members of your immediate family (your spouse or equivalent and dependents) generally must follow the same rules that you do. For example, your spouse's investments must be investments that you could own under the rules. This rule applies even if your spouse keeps the investments in his or her own name or with a different broker.

This general rule has the following two exceptions:

- Your immediate family member's employment with a client would not impair your firm's independence, provided he or she is not in a key position.
- Immediate family members of certain covered members may invest in a client through an employee benefit plan (for example, retirement or savings account), provided the plan is normally offered equitably to all similar employees. The covered members whose families may invest in this way are the following:
  - Partners and managers who provide only nonattest services to the client
  - Partners who are covered members *only* because they practice in the same office where the client's lead attest partner practices in connection with the engagement

In other words, immediate family of individuals on the attest engagement team or of those who can influence the attest engagement team *may not* invest in a client under any circumstances.

Under SEC rules, the immediate family of certain covered persons may have financial interests in SEC audit clients only if such interests are an unavoidable consequence of their participation in an employee compensation or benefit plan. This means that if nonclient investments are available through the plan, the immediate family member must choose those investments.

### *What About My Other Close Relatives?*

The close relatives (siblings, parents, and nondependent children) of most covered members are subject to some employment and financial restrictions. Your close relative's employment by a client in a key position impairs independence, except for covered members who provide only nonattest services to a client.

Rules pertaining to your close relatives' financial interests differ depending on why you are considered a covered member:

- If you are a covered member because you participate on the client's attest engagement team, your independence would be considered to be impaired if you are aware that your close relative has a financial interest in the client that either
  - was material to your relative's net worth or
  - enables the relative to exercise significant influence over the client.

- If you are a covered member because you are able to influence the client's attest engagement or are a partner in the office in which the lead attest engagement partner practices in connection with the engagement, your independence will be impaired if you are aware that your close relative has a financial interest in the client that
  - is material to your relative's net worth and
  - enables your relative to exercise significant influence over the client.

Under SEC rules, your close family members include your spouse (or equivalent) and dependents and your parents, nondependent children, and siblings. If you are a covered person, your independence is affected if your close family member

- has an accounting role or financial reporting oversight role with the SEC audit client (for example, the family member is a treasurer, CFO, accounting supervisor, or controller) or
- owns more than 5 percent of a client's equity securities or controls the client.

In addition, independence is considered to be impaired if any partner's close family member controls an SEC audit client.

## Financial Relationships

### *When Do My (or My Family's) Financial Interests Impair Independence?*

This section discusses various types of financial relationships and how they affect independence. Although this section focuses on how these rules apply to you and your family, keep in mind that your firm also is subject to the financial relationship rules (because firms are included in the AICPA definition of *covered member*).

As a covered member, you (and your spouse or equivalent and dependents) are not permitted to have the following:

- A direct financial interest in that client, regardless of how immaterial it would be to your net worth
- A material indirect financial interest in that client

**Note:** The code does not define or otherwise provide guidance on determining materiality. In determining materiality, you should apply professional judgment to all relevant facts and circumstances and refer to applicable guidance in the professional literature. Both qualitative and quantitative factors should be considered.

In addition, if you commit to acquire a direct or material indirect financial interest in a client, your independence would be impaired. For example, if you sign a stock subscription agreement with the client, your independence would be considered impaired as soon as you sign the agreement.

Examples of financial interests include shares of stock; mutual fund shares; debt security issued by an entity; partnership units; stock rights; options or

## 30

### Other Alerts

warrants to acquire an interest in a client; or rights of participation such as puts, calls, or straddles.

The following types of financial interests are *direct financial interests*:

- Owned by you directly
- Under your control
- Beneficially owned<sup>9</sup> by you through an investment vehicle, estate, trust, or other intermediary if you can either
  - control the intermediary or
  - have the authority to supervise or participate in the intermediary's investment decisions.

For example, if you invest in a participant directed 401(k) plan, whereby you are able to select the investments held in your account or are able to select from investment alternatives offered by the plan, you would be considered to have a direct financial interest not only in the 401(k) plan but also in the investments held in your account.

You also have a direct financial interest in a client if you have a financial interest in a client through one of the following:

- A partnership, if you are a general partner
- A Section 529 savings plan, if you are the account owner
- An estate, if you serve as an executor and meet certain other criteria
- A trust, if you serve as the trustee and meet certain other criteria

For example, suppose you are a covered member with respect to ABC Co., and you are also a general partner of XYZ Partnership. XYZ Partnership owns shares in ABC Co. Under the independence rules, you would be deemed to have a direct financial interest in ABC Co., which would impair your independence, regardless of materiality.

An indirect financial interest arises if you have a financial interest that is beneficially owned through an investment vehicle, estate, trust, or other intermediary when you can neither control the intermediary nor have the authority to supervise or participate in the intermediary's investment decisions.

For example, if you invest in a defined contribution plan that is not participant directed and you have no authority to supervise or participate in the plan's investment decisions, you would be considered to have an indirect financial interest in the underlying plan investments, in addition to a direct financial interest.

**Note:** Interpretation No. 101-15, "Financial Relationships," under Rule 101 (AICPA, *Professional Standards*, vol. 2, ET sec. 101 par. .17), provides extensive examples of various types of financial interests and whether they should be considered to be direct or indirect financial interests, including investments in mutual funds, retirement and

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<sup>9</sup> A financial interest is beneficially owned if an individual or entity is not the record owner of the interest but has a right to some or all of the underlying benefits of ownership. These benefits include the authority to direct the voting or the disposition of the interest or to receive the economic benefits of the ownership of the interest.

savings plans, Section 529 plans, trusts, partnerships, and insurance products.

The SEC classifies your investment in an SEC audit client held through another entity (the intermediary) as direct if either of the following is true:

- You participate in the intermediary's investment decisions or have control over them.
- The investment in the client by the intermediary (which is not a diversified mutual fund) represents 20 percent or more of the value of its total investments.

If neither of the preceding applies, your investment in an SEC audit client through another entity would normally be considered to be an indirect financial interest in that client.

***What if My Immediate Family or I Receive a Financial Interest as a Result of an Inheritance or a Gift?***

If, due to an unexpected event, you or members of your immediate family receive a financial interest in an attest client that would impair your independence, you may qualify under an exemption in the rules if you meet the following criteria:

- The financial interest was unsolicited.
- You dispose of the interest as soon as practicable but no later than 30 days after you become aware of it and have the right to dispose.
- If you do not have the right to dispose of the interest (for example, as in the case of stock options or restricted stock), you do not participate in the attest engagement for the client.

***What Are the Rules That Apply to My Mutual Fund Investments (and Those of My Family) if My Firm Audits Those Mutual Funds?***

If you are a covered member with respect to a mutual fund attest client of your firm and you or your immediate family own shares in the fund, you have a direct financial interest in the fund client.

The SEC rules also prohibit the firm and covered persons and their immediate family members from having any financial interest in an entity (even one that is not a client) that is part of an investment company complex that includes an SEC audit client.

***Which Rules Pertain to My Mutual Fund Investments (and Those of My Family) if My Firm Audits Companies Held in Those Mutual Funds?***

Financial interests that you and your immediate family have in clients through a mutual fund are considered to be indirect financial interests in those clients unless the fund is a diversified mutual fund.

If a mutual fund is diversified and you or your immediate family, or both, own 5 percent or less of its outstanding shares, the fund's holdings in clients for which you are a covered person will *not* be considered material indirect financial



## 32

### Other Alerts

interests in those clients. Thus, you would be relieved of the burden of having to monitor whether, and to what degree, the fund invests in audit clients for which you are a covered person.

If the fund is not diversified or you or your family, or both, own more than 5 percent of the fund's equity, you should treat the fund's holdings as indirect financial interests.

For example, suppose ABC Mutual Fund, a diversified mutual fund, owns shares in a client, XYZ, and

- ABC Mutual Fund's net assets are \$10,000,000;
- your shares in ABC Mutual Fund are worth \$50,000;
- ABC Mutual Fund has 10 percent of its assets invested in XYZ; and
- your indirect financial interest in XYZ is \$5,000 ( $\$50,000 \times .10$ ).

If \$5,000 is material to your net worth, independence would be considered to be impaired.

#### ***May I Have a Joint Closely Held Investment With a Client?***

As a covered member, if you or the client individually or collectively controls an investment, that investment is considered to be a joint closely held investment. If this joint closely held investment is material to your net worth, independence would be considered to be impaired. In this rule, the term *client* includes certain persons associated with the client, such as officers, directors, or owners who are able to exercise significant influence over the client.

The SEC rules prohibit you and your immediate family from having a joint business venture with an SEC audit client or with persons associated with the client in a decision making capacity (meaning officers, directors, or substantial shareholders), regardless of whether the venture is material to your net worth. The SEC believes that these joint ventures, whether material or not, cause the client and the audit firm to have mutuality of interests, which impairs independence.

#### ***May My Family or I Borrow Money From or Lend Money to a Client?***

If you are a covered member with respect to an attest client, you and your immediate family may not have a loan to or from the following:

- The client
- An officer or director of the client
- An individual holding 10 percent or more of the client's outstanding equity securities (or other ownership interests)

Certain exceptions affect this rule. First, specific loans exist that covered members are permitted to have from financial institution attest clients. They are the following:

- Car loans and leases collateralized by the vehicle
- Credit card and overdraft reserve account balances that are kept current and do not exceed \$10,000 (by payment due date, including any grace period)

### Independence and Ethics Developments—2009

33

- Passbook loans fully collateralized by cash deposits at the same financial institution
- Loans fully collateralized by an insurance policy

In addition, if you have a loan from a client financial institution (a bank, for example) that meets certain criteria, your loan may be grandfathered (that is, you may be allowed to keep it). For your loan to be grandfathered, you must have obtained it under normal lending procedures, terms, and requirements. The following loans may be grandfathered:

- Home mortgages
- Other secured loans
- Unsecured loans that are immaterial to your net worth

Generally speaking, a loan may be grandfathered if you obtained it before any of the following:

- You became a covered member with respect to the client
- The financial institution became a client
- The client acquired the loan

To maintain your loan's grandfathered status, you must keep the loan current (that is, make timely payments according to the loan agreement). Also, you cannot renew or renegotiate the terms of the loan (for example, the interest rate or formula) unless the change was part of the original agreement (for example, an adjustable rate mortgage).

The SEC rules differ from the AICPA rules in that secured loans (other than a mortgage on your primary residence) and immaterial unsecured loans may not be grandfathered.

### ***May I Have a Brokerage Account With a Client?***

The AICPA rules indicate that for independence to be maintained, a covered member whose assets are held by a broker-dealer client must not receive any preferential treatment or terms, and any assets that are subject to risk of loss must be immaterial to the covered member's net worth. In addition, margin accounts may be subject to the preceding loan rules.<sup>10</sup>

Under the SEC rules, you may have a brokerage account with an SEC audit client if your account (1) only holds cash or securities and (2) is fully insured by the Securities Investor Protection Corporation.

### ***May I Have a Bank Account With a Client?***

As a covered member, you may have a bank account with a client financial institution (for example, checking, savings, money market accounts, and certificates

<sup>10</sup> See the preceding question "May My Family or I Borrow Money From or Lend Money to a Client?" in the "Financial Relationships" section.

## 34

### Other Alerts

of deposit) if your deposits are fully insured by state or federal deposit insurance agencies or if uninsured amounts are not material to your net worth.<sup>11</sup>

The SEC prohibits covered persons and their immediate families from having bank account balances in excess of Federal Deposit Insurance Corporation (FDIC) insurance limits. That is, deposits in excess of FDIC limits are considered to impair independence even if the amounts are immaterial to you and your family.<sup>12</sup>

### ***May I Have an Insurance Policy With a Client?***

The AICPA rules<sup>13</sup> indicate that, to maintain independence, a covered member must not receive any preferential treatment or terms when purchasing an insurance policy from a client. If the policy has an investment option, the financial interest rules must be applied.

The SEC prohibits covered persons and their immediate family members from owning an individual insurance policy issued by an SEC audit client unless both of the following criteria are met:

- He or she obtained the policy before the professional became a covered person.
- The likelihood of the insurer becoming insolvent is remote

### ***May I Give Gifts or Entertainment to or Accept Gifts or Entertainment From a Client?***

An ethics ruling<sup>14</sup> addresses the exchange of gifts and entertainment among covered members, the attest client, and certain persons associated with the client (for example, persons in key positions and persons owning 10 percent or more of the client's outstanding equity securities or other ownership interests).

Independence is impaired if the firm, a member of the attest engagement team, or a person able to influence the engagement accepts a gift that is not clearly insignificant.

A covered member may give a gift to persons associated with the client and not impair independence if the gift is reasonable in the circumstances. In addition, covered members may give or receive entertainment, provided it was reasonable in the circumstances.

<sup>11</sup> Both AICPA and SEC rules permit a practical exception for firms that maintain deposits exceeding insured limits when the likelihood of the financial institution experiencing financial difficulties is considered remote.

<sup>12</sup> The SEC treats money market funds (as opposed to money market accounts) as mutual funds for the purposes of their rules. Also see Rule 2-01(c)(1)(B).

<sup>13</sup> The guidance is found in the "Insurance Products" portion of Interpretation No. 101-15, "Financial Relationships," under Rule 101 (AICPA, *Professional Standards*, vol. 2, ET sec. 101 par. .17).

<sup>14</sup> See Ethics Ruling No. 114, "Acceptance or Offering of Gifts and Entertainment to or From an Attest Client," of ET section 191, *Ethics Rulings on Independence, Integrity, and Objectivity* (AICPA, *Professional Standards*, vol. 2, ET sec. 191 par. .228–.229).

Another ethics ruling<sup>15</sup> addresses the broader issue of integrity and objectivity when partners, professionals, or their firms exchange gifts or entertainment with clients or persons associated with clients. Generally, gifts are differentiated from entertainment by whether the client participates in the activity with the firm member (for example, giving tickets to a sporting event for the client to use would be considered a gift versus attending the event with the client, which would be considered entertainment).<sup>16</sup>

Relevant factors in determining *reasonableness* include the event or occasion (if any) giving rise to the gift or entertainment, cost or value, frequency, whether business was conducted, and who participated.

## Business Relationships

### *Which Business Relationships With a Client Impair Independence?*

As a partner or professional employee of your firm, independence would be considered to be impaired if you entered into certain business relationships with an attest client of the firm. Accordingly, you may not serve a client as any of the following:

- Employee, director, officer, or in any management capacity
- Promoter, underwriter, or voting trustee
- Stock transfer or escrow agent
- General counsel (or equivalent)
- Trustee for a client's pension or profit sharing trust

In essence, any time you are able to make management decisions on behalf of a client or exercise authority over a client's operations or business affairs, independence is impaired.

Your independence is considered impaired even if you were a volunteer board member because you would be part of the client's governing body and, therefore, would be able to participate in the client's management decisions.

Two possible exceptions apply to this rule:

- If you are an honorary director or trustee for a client that is a nonprofit charitable, civic, or religious organization, you may hold such position with a client if
  - your position is purely honorary,
  - you do not vote or participate in managing the organization, or
  - your position is clearly identified as honorary in any internal or external correspondence.
- In addition, you may serve on a client's advisory board if all of the following criteria are met:

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<sup>15</sup> See Ethics Ruling No. 113, "Acceptance or Offering of Gifts or Entertainment," of ET section 191 (AICPA, *Professional Standards*, vol. 2, ET sec. 191 par. .226–.227).

<sup>16</sup> See [www.aicpa.org/download/ethics/Gifts\\_Basis\\_Document.pdf](http://www.aicpa.org/download/ethics/Gifts_Basis_Document.pdf).

## 36

### Other Alerts

- The board's function is purely advisory.<sup>17</sup>
- The board does not appear to make decisions for the client.
- The advisory board and any decision making boards are separate and distinct bodies.
- Common membership between the advisory board and any decision making groups is minimal.

The SEC prohibits direct or material indirect business relationships with an SEC audit client (or persons associated with a client), except when the firm is acting as a consumer in the ordinary course of business (for example, purchasing goods or services from a client at normal commercial terms, and these goods or services will be consumed by the firm). Examples of prohibited business relationships include joint business ventures, limited partnership agreements, and certain leasing interests.

## Nonattest Services

### ***Which Rules Describe the Nonattest Services That My Firm and I May or May Not Provide to Attest Clients?***

The term *nonattest services* includes accounting, tax, and consulting services that are not part of an attest engagement.<sup>18</sup> Nonattest services specifically addressed in the rules are the following:

- Bookkeeping services
- Nontax disbursement services
- Internal audit assistance
- Benefit plan administration
- Investment advisory or management services
- Tax compliance services
- Corporate finance consulting or advisory services
- Appraisal, valuation, or actuarial services
- Executive or employee search services
- Business risk consulting
- Information systems design, installation, or integration
- Forensic accounting services

<sup>17</sup> When evaluating your independence under this rule, you should examine the applicable board or committee charter to determine whether it is consistent with this ethics ruling.

<sup>18</sup> Defined in the AICPA Code of Professional Conduct, an *attest engagement* is one that requires independence under AICPA *Professional Standards*; for example, audits and reviews of financial statements or agreed-upon procedures performed under the attestation standards are considered attest engagements.

In addition to considering the general standard and four guiding principles, the SEC rules generally prohibit a CPA from providing the following services to an SEC audit client during the audit and professional engagement period:

- Bookkeeping and other services related to the client's accounting records or financial statements
- Financial information systems design and implementation
- Appraisal or valuation services
- Actuarial services
- Internal audit outsourcing
- Management functions
- Human resources
- Broker-dealer, investment adviser, or investment banking
- Legal services
- Expert services unrelated to the audit

Under PCAOB rules, the following types of services also are subject to significant restrictions if the auditor provides them to an issuer during the audit and professional engagement period:

- Aggressive or confidential tax transactions
- Personal tax services provided to persons in financial reporting oversight roles

If your firm performs nonattest services for an attest client, the independence rules impose limits on the nature and scope of the services that your firm may provide. In other words, the extent to which your firm may perform certain tasks will be limited by the rules. Further, certain services will be prohibited in total (for example, serving as a client's general counsel). These rules apply during the period of the professional engagement and the period covered by the financial statements (to which the attest services relate). In addition, the AICPA staff issued a frequently asked question (FAQ), "Period of the Professional Engagement," which clarifies how the rules apply to nonattest services provided to a new attest client prior to the time of engagement.

In August 2007, the SEC staff updated its FAQ document titled *Office of the Chief Accountant: Application of the Commission's Rules on Auditor Independence Frequently Asked Questions*. FAQ No. 7 under "Prohibited and Non-audit Services" addresses the question of whether a successor auditor who performed one of the preceding services during the audit period (period covered by the financial statements) would be independent of an SEC audit client. The FAQ states that if the services (a) relate solely to the prior period audited by the predecessor auditor and (b) were performed before the successor auditor was engaged to audit the current audit period, independence would not be impaired.

This section does not discuss each of these services, but rather focuses on a few for purposes of illustration. To see the full context of the rules, see Interpretation No. 101-3, "Performance of Nonattest Services," under Rule 101 (AICPA, *Professional Standards*, vol. 2, ET sec. 101 par. .05), and SEC Rule 2-01(c)(4), "Non-audit services." You also are encouraged to review the Nonattest Services

## 38

### Other Alerts

FAQs developed by the Professional Ethics Division and the Prohibited and Non-audit Services FAQs developed by the SEC's Office of the Chief Accountant.

The AICPA rules require a member to comply with more restrictive independence provisions, if applicable, of certain regulators, such as state boards of accountancy and the SEC, GAO, and DOL.

SEC and PCAOB rules require independence of an issuer that is an audit client and various affiliated entities of the client.<sup>19</sup>

**Note:** SEC rules also require a client's audit committee (or equivalent) to preapprove all audit and nonaudit services provided by the firm to an issuer and the issuer's consolidated entities. Proposals to provide tax or internal control-related services are subject to more extensive audit committee preapproval requirements under PCAOB Rule 3524, *Audit Committee Pre-approval of Certain Tax Services*, and Rule 3525, *Audit Committee Pre-approval of Non-audit Services Related to Internal Control Over Financial Reporting* (AICPA, *PCAOB Standards and Related Rules*, Rules of the Board, "Rules"), respectively.

PCAOB Rule 3526, *Communication with Audit Committees Concerning Independence* (AICPA, *PCAOB Standards and Related Rules*, Rules of the Board, "Rules"), superseded the PCAOB's interim standard, ISB Standard No. 1, *Independence Discussions with Audit Committees* (AICPA, *PCAOB Standards and Related Rules*, PCAOB Standards, As Amended, "Independence Standards Board"), and its interpretations. Before accepting a new audit engagement and annually thereafter, the auditor must describe in writing to the issuer's audit committee all relationships between the auditor and the client (including affiliates of both) that could reasonably be thought to bear on independence, discuss these matters with the audit committee, and document the substance of that discussion (effective September 30, 2008).

### AICPA General Requirements

#### General Requirement No. 1

One of the key principles underlying the AICPA rules on nonattest services is that you may not serve—or even appear to serve—as a member of a client's management. For example, you may not do any of the following:

- Make operational or financial decisions for the client
- Perform management functions for the client
- Report to the board of directors on behalf of management

In addition, the following are examples of the types of activities that impair independence:

- Authorizing or executing a transaction on behalf of a client
- Preparing the client's source documents (for example, purchase orders)
- Having custody of a client's assets
- Establishing or maintaining internal controls, including monitoring ongoing activities

<sup>19</sup> See Rule 2-01(f)(4) and (6).



### *General Requirement No. 2*

To help ensure compliance with the first general requirement, the second requirement states that the client must agree to assume certain responsibilities related to the nonattest services engagement. So, prior to agreeing to perform any nonattest services for the client, the firm must obtain the client's agreement to

1. make all management decisions and perform all management functions;
2. designate an individual who possesses suitable skill, knowledge, and experience, preferably within senior management, to oversee the services;
3. evaluate the adequacy and results of the services performed; and
4. accept responsibility for the results of the services.

With regard to item 2 in the preceding list, the firm should be satisfied that the client's designee sufficiently understands the services to be performed to oversee them. This does not mean that the individual must be able to perform or reperform the services. It means that he or she should be able to understand and agree to the nature, objectives, and scope of the services; make all significant judgments; evaluate the adequacy and results of the service; accept responsibility for the service results; and ensure that the resulting work product meets the agreed-upon specifications. The client also must be willing to commit the time and resources needed for the designee to fulfill these duties.

### *General Requirement No. 3*

Before performing nonattest services, the firm should establish and document its understanding with the client regarding the following:

- Objectives of the engagement
- Services to be performed
- Client's acceptance of its responsibilities
- Member's responsibilities
- Any limitations of the engagement

The firm should document the understanding in the engagement letter, audit planning memo, or other internal firm file.

**Note:** Routine activities (for example, assisting clients with technical accounting questions, advising on internal controls, or providing periodic training on new pronouncements) that are part of the normal member-client relationship are exempt from the second and third general requirements.

### ***What Are the Rules Concerning Performing Bookkeeping Services for a Client?***

The AICPA independence rules prohibit members from acting as client management in all circumstances. Accordingly, a member may provide bookkeeping services if the client oversees the services and, among other things, performs all management functions and makes all management decisions in connection with the services. For example, if a member is engaged to provide bookkeeping

## 40

### Other Alerts

services that will result in a set of financial statements, the client must do the following:

- Approve all account classifications
- Provide source documents to the member so that the member can prepare journal entries
- Take responsibility for the results of the member's services (for example, financial statements)

**Note:** Proposing adjusting entries to a client's financial statements as a part of the member's audit, review, or compilation services is considered a normal part of those engagements and would not be considered the performance of a nonattest service subject to the general provisions of Interpretation No. 101-3, provided the client reviews these entries, understands the impact on its financial statements and records any adjustments identified by the member.

Because of self-audit concerns, performing any type of bookkeeping service for an SEC audit client is considered to impair independence under SEC rules unless it is reasonable to expect that the results of the auditor's services will not be subject to the firm's audit procedures. The SEC considers there to be a rebuttable presumption that the results of these services would be subject to audit procedures, and, therefore, the firm must overcome the presumption to perform the service.

This presumption of self audit also applies to (1) financial information design and implementation; (2) appraisals, valuations, fairness opinions, or contribution-in-kind reports; (3) actuarial-related advisory services; and (4) internal audit outsourcing

### *May My Firm Provide Internal Audit Assistance to a Client?*

To perform internal audit assistance for a client and maintain independence, your firm may not act—or appear to act—as a member of the client's management. For example, you and your firm may not do the following:

- Make decisions on the client's behalf
- Report to the client's governing body

To maintain independence, the client must do the following:

- Designate an individual or individuals who possess suitable skill, knowledge, and experience to oversee the internal audit function
- Determine the scope, risk, and frequency of internal audit activities
- Evaluate the findings and results of internal audit activities
- Evaluate the adequacy of the audit procedures performed and related findings

Internal audit services provided to an SEC audit client impair independence unless it is reasonable to expect that the results of the auditor's services would not be subject to the firm's audit procedures.

**Note:** For entities regulated by the FDIC or other banking agencies, see [www.fdic.gov/news/news/financial/2009/fil09033.html](http://www.fdic.gov/news/news/financial/2009/fil09033.html).

### ***May My Firm Provide Valuation, Appraisal, or Actuarial Services to a Client?***

Your firm may not provide valuation, appraisal, or actuarial services to a client if

- the results of the service would be material to the client's financial statements and
- the service involves a significant amount of subjectivity.

For instance, your firm may not perform a valuation in connection with a business combination that would have a material effect on a client's financial statements because that service involves significant subjectivity (for example, setting the assumptions and selecting and applying the valuation methodology).

Two limited exceptions to this rule apply. First, valuation, appraisal, or actuarial services performed for nonfinancial statement purposes may be provided if they otherwise meet the rule's general requirements (for example, the client assigns an individual who is in a position to make an informed judgment on and accept responsibility for the results of the service to oversee the service). Also, your firm may provide an actuarial valuation of a client's pension or postretirement liabilities because the results of the valuation would be reasonably consistent, regardless of who performs the valuation.

The SEC prohibits your firm from providing valuation, appraisal, or any service involving a fairness opinion or contribution-in-kind report<sup>20</sup> to an SEC audit client unless it is reasonable to expect that your firm would not audit the results of those services.

In August 2008, the staff of the Professional Ethics Division issued nonauthoritative guidance (in the form of an FAQ) on the question of whether, under Interpretation No. 101-3, members could assist an attest client in applying Financial Accounting Standards Board (FASB) *Accounting Standards Codification*<sup>TM</sup> (ASC) 805, *Business Combinations*, or FASB ASC 350, *Intangibles—Goodwill and Other*, while maintaining independence. Specifically, the FAQ addresses whether the following services would be considered to impair independence:

- Providing the client advice on valuation methodologies and assumptions needed to perform the valuation
- Providing advice on valuation templates, software or other tools that allow the client to determine an appropriate value for acquired assets, goodwill, contingent consideration, and so on

### ***May My Firm Provide Investment Advisory Services to a Client?***

Here are examples of what you and your firm may do under the AICPA rules:

- Make recommendations to a client about the allocation of funds to various asset classes
- Analyze investment performance

<sup>20</sup> Per the SEC, fairness opinions and contribution-in-kind reports are opinions and reports in which your firm provides its opinion on the adequacy of consideration in a transaction.

## 42

### Other Alerts

However, the AICPA rules also indicate that you and your firm may not do the following:

- Make investment decisions for the client
- Execute investment transactions
- Take custody of a client's assets

### ***May My Firm Design or Implement an Information System for a Client?***

Your firm may not design or develop a client's financial information system or make more than insignificant modifications to the source code underlying such a system. In addition, operating a client's local area network is prohibited.

Your firm may install an accounting software package for a client, including helping the client set up a chart of accounts and financial statement format. Your firm also may provide training to the client's employees on how to use an information system. Your firm may not, however, supervise the client's employees in their day-to-day use of the system because that activity is a management function.

Your firm is not precluded from designing, implementing, integrating, or installing an information system that is unrelated to the client's financial reporting process.<sup>21</sup>

SEC rules prohibit your firm from providing any service related to an SEC audit client's financial information system design or implementation unless the results of your firm's services would not be subject to audit procedures during an audit of the client's financial statements. Your firm may do either of the following:

- Evaluate internal controls of a financial information system as it is being designed, implemented, or operated for the client by another service provider
- Make recommendations on internal control matters to management in connection with a system design and implementation project being performed by another service provider

**Note:** If your audit client is an issuer, your firm must obtain preapproval for these and other internal control-related services, in accordance with PCAOB Rule 3525.

### Fee Issues

### ***What Types of Fee Arrangements Between My Firm and a Client Are Prohibited?***

Two types of fee arrangements, contingent fees and commissions, are prohibited if the arrangement involves certain attest clients, even though the fee is not related to an attest service.

<sup>21</sup> Frequently asked questions are available to assist members in understanding and implementing the new information technology services provisions and may be obtained at [www.aicpa.org/Professional+Resources/Professional+Ethics+Code+of+Professional+Conduct/Professional+Ethics/Resources+and+Tools/Frequently+Asked+Questions.htm](http://www.aicpa.org/Professional+Resources/Professional+Ethics+Code+of+Professional+Conduct/Professional+Ethics/Resources+and+Tools/Frequently+Asked+Questions.htm).

A *contingent fee* is an arrangement whereby (1) no fee is charged unless a specified result is attained or (2) the amount of the fee depends on the results of your firm's services. Some examples of contingent fees are the following:

- Your firm receives a "finder's fee" for helping a client locate a buyer for one of your client's assets.
- Your firm performs a consulting engagement to decrease a client's operating costs. The fee is based on a percentage of the cost reduction that the client achieves as a result of your service.

The following are exceptions:

- Fees fixed by a court or other public authority
- In tax matters, fees based on the results of judicial proceedings or the findings of governmental agencies

A *commission* is any compensation paid to you or your firm for (1) recommending or referring a third party's product or service to a client or (2) recommending or referring a client's product or service to a third party.

The following are examples of commissions:

- If you or your firm refers a client to a financial planning firm that pays you a commission for the referral
- If you or your firm sells accounting software to a client and receives a percentage of the sales price (a commission) from a software company
- If you or your firm refers a nonclient to an insurance company client, which pays you a percentage of any premiums subsequently received (a commission) from the nonclient.

Commissions or contingent fee arrangements with a client are not allowed if your firm also provides one of the following services to a client:

- An audit of financial statements
- A review of financial statements
- A compilation of financial statements if a third party (for example, a bank or investor) will rely on the financial statements and the report does not disclose a lack of independence
- An examination of prospective financial statements

You may have commission and contingent fee arrangements with persons associated with a client—such as officers, directors, and principal shareholders—or with a benefit plan that is sponsored by a client (that is, the plan itself is not an attest client). For example, you may receive a commission from a nonclient insurer if you refer an officer of an attest client to the insurer and the officer purchases a policy. Even though this situation is permitted, you are still required to tell the officer that you received a commission for making the referral.

**Note:** State boards of accountancy and state societies also may have more restrictive regulations regarding fee arrangements, as well as specific disclosure requirements.

PCAOB Rule 3521, *Contingent Fees* (AICPA, *PCAOB Standards and Related Rules*, Rules of the Board, "Rules"), prohibits you and your firm from providing any service or product to an SEC audit client for a contingent fee or commission or receiving from the audit client, directly or indirectly, a contingent fee or commission. Although the PCAOB's definition of contingent fees was adapted from the SEC's definition, the PCAOB rule eliminated the exception for fees in tax matters, if determined based on the results of judicial proceedings or the findings of governmental agencies. In addition, the PCAOB rule specifically indicates that the contingent fees cannot be received directly or indirectly from an issuer that is an audit client.

### ***When Are Referral Fees Permitted?***

The AICPA rule provides an exception for referral fees for recommending or referring a CPA's services to another person or entity. That is, you may (1) receive a fee for referring a CPA's services to any person or entity or (2) if you are a CPA, you may pay a fee to obtain a client. You must inform the client if you receive or pay a referral fee.

### ***Is Independence Affected When a Client Owes the Firm Fees for Professional Services That the Firm Has Already Provided?***

If a client owes your firm fees for services rendered more than one year ago, your firm's independence is considered impaired. It does not matter if the fees are related to attest services; what matters is that the client has an outstanding debt with the firm. This is the case even if the client has given you a note receivable for these fees.

The SEC generally expects payment of past due fees before an engagement has begun, although a short term payment plan may be accepted if the SEC audit client has committed to pay the balance in full before the current year report is issued.<sup>22</sup>

### ***Does Being Compensated for Selling Certain Services to Clients Affect My Independence?***

The AICPA rules do not specifically address this issue.

The SEC prohibits audit partners from being directly compensated for selling nonattest services to issuers that are audit clients. The SEC believes that such financial incentives could threaten an audit partner's objectivity and that the appearance of independence could be affected by such compensation arrangements.<sup>23</sup>

The rule does not prevent an audit partner from sharing in profits of the audit practice or the overall firm. Nor does it preclude the firm from evaluating a partner based on factors related to the sale of nonaudit services to issuers (for example, the complexity of engagements or overall management of audit or nonaudit engagements).

<sup>22</sup> The exception generally has been applied only to engagements to audit a client's financial statements included in its annual report, not in a registration statement.

<sup>23</sup> Accounting firms with 10 or fewer partners and 5 or fewer audit clients that are issuers, as defined by the SEC, are exempt from this rule.

***Does It Matter if a Significant Proportion of My Firm's Fees Come From a Particular Client?***

The conceptual framework states that a financial self-interest threat may exist due to "excessive reliance on revenue from a single attest client." In addition, Rule 102 and ET section 55, *Article IV—Objectivity and Independence* (AICPA, *Professional Standards*, vol. 2), discuss in broad terms that members should be alert for relationships that could diminish their objectivity and independence in performing attest services. The significance of a client to a member (or his or her firm)—measured in terms of fees, status, or other factors—may diminish a member's ability to be objective and maintain independence when performing attest services.

To address this issue, firms should consider implementing the following policies and procedures to identify and monitor significant clients to help mitigate possible threats to a member's objectivity and independence:

- Policies and procedures for identifying and monitoring significant client relationships, including the following:
  - Considering client significance in the planning stage of the engagement.
  - Basing the consideration of client significance on firm specific criteria or factors that are applied on a facts-and-circumstances basis (see the "Factors to Consider in Identifying Significant Clients" section that follows).
  - Periodically monitoring the relationship. What constitutes periodic is a matter of judgment, but assessments of client significance that are performed at least annually can be effective in monitoring the relationship. During the course of such a review, a client previously deemed to be significant may cease to be significant. Likewise, clients not identified as significant could become significant whenever factors that the firm considers relevant for identifying significant clients arise (for example, additional services are contemplated).
- Policies and procedures for helping mitigate possible threats to independence and objectivity, including the following:
  - Assigning a second (or concurring) review partner who is not otherwise associated with the engagement and practices in an office other than those that perform the attest engagement
  - Subjecting the assignment of engagement personnel to approval by another partner or manager
  - Periodically rotating engagement partners
  - Subjecting significant client attest engagements to internal firm monitoring procedures
  - Subjecting significant client attest engagements to preissuance or postissuance reviews or the firm's external peer review process



## 46

### Other Alerts

The most effective safeguards that a firm can employ will vary significantly, depending on the size of the firm; the way the firm is structured (for example, whether highly centralized or departmentalized); and other factors. For example, smaller firms (particularly those with one office) tend to be simpler and less departmentalized than larger firms. Generally, their processes will be less formal and involve fewer people than those of larger firms. Further, the firms' managing partners may engage in frequent and direct communications with the firms' partners and professional staff on client matters and be personally involved in staff assignments. Larger firms draw from a sizeable and diverse talent pool. In those firms, partners who are not affiliated with the engagement (or the client service office or business unit) can choose second (or concurring) review partners from outside the office performing the attest engagement. Mid-sized or regional firms may have aspects of both their smaller and larger counterparts, like combining the ability to choose second review partners from an office other than the client service office while maintaining a relatively close connection to specific client relationships.

### ***Factors to Consider in Identifying Significant Clients***

The following are both qualitative and quantitative factors that can reveal a significant client:

- The size of the client in terms of the percentage of fees or the dollar amount of fees versus total revenue of the engagement partner, office, or practice unit of the firm<sup>24</sup>
- The significance of the client to the engagement partner, office, or practice unit of the firm in light of the following:
  - The amount of time the partner, office, or practice unit devotes to the engagement
  - The effect on the partner's stature within the firm due to his or her relationships with the client
  - The manner in which the partner, office, or practice unit is compensated
  - The effect that losing the client would have on the partner, office, or practice unit
- The importance of the client to the firm's growth strategies (for example, the firm is trying to gain entry into a particular industry)
- The stature of the client, which may enhance the firm's stature (for example, the firm is trying to gain entry into a particular industry)
- Whether the firm also provides services to related parties (for example, also provides professional services to affiliates or owners of the client)
- Whether the engagement is recurring

Judgment is necessary to determine whether a client is significant to the firm, office, practice unit, or partner of the firm. Firms will vary considerably in terms of the degree to which they consider some factors to be more pertinent

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<sup>24</sup> Assessing client significance at the business or practice unit level may be a more meaningful measure for firms that structure their practices along industry lines (such as healthcare or financial services).

than others. Gauges that relate to each relevant level within a firm (for example, firm, geographic region, office, or practice unit) may be useful but likely will be different for various levels within the firm.

In general, if a firm derives more than 15 percent of its total revenues from one SEC audit client or group of related clients, independence may be impaired because this may cause the firm to be overly dependent on the client or group of related clients.

## Further Assistance

### *Where Can I Find Further Assistance With My Independence Questions?*

This appendix does not address many subjects included in the AICPA rules. Readers are encouraged to view the online version of the code at [www.aicpa.org/about/code/index.html](http://www.aicpa.org/about/code/index.html).

In addition, readers should refer to ET section 100.01 in evaluating whether a specific circumstance that is not addressed in the code would pose an unacceptable threat to independence.

As specific services and situations arise in practice, refer to the independence literature and consult with those responsible for independence in your firm. If you need further assistance researching your question, contact one of the following organizations for guidance.

The AICPA has a variety of resources for practitioners:

- For information about the AICPA's ethics standard setting activities, see [www.aicpa.org/Professional+Resources/Professional+Ethics+Code+of+Professional+Conduct/Professional+Ethics/Exposure+Drafts+-+Standard+Setting/](http://www.aicpa.org/Professional+Resources/Professional+Ethics+Code+of+Professional+Conduct/Professional+Ethics/Exposure+Drafts+-+Standard+Setting/).
- For resources related to understanding and applying nonattest services rules, see [www.aicpa.org/Professional+Resources/Professional+Ethics+Code+of+Professional+Conduct/Professional+Ethics/Resources+and+Tools/](http://www.aicpa.org/Professional+Resources/Professional+Ethics+Code+of+Professional+Conduct/Professional+Ethics/Resources+and+Tools/).
- For the *Background and Basis for Conclusions* document for nonattest services, see [www.aicpa.org/download/ethics/Basis\\_for\\_Conclusions\\_Non\\_Attest\\_Services.pdf](http://www.aicpa.org/download/ethics/Basis_for_Conclusions_Non_Attest_Services.pdf).
- The AICPA code is available at [www.aicpa.org/about/code/index.html](http://www.aicpa.org/about/code/index.html).
- For independence inquiries by phone, call (888) 777-7077. Send e-mail inquiries to [ethics@aicpa.org](mailto:ethics@aicpa.org).
- The AICPA interactive CD-ROM course on independence, *Independence*, teaches the AICPA and SEC independence rules and qualifies for eight hours of continuing professional education credits. See [www.cpa2biz.com/AST/Main/CPA2BIZ\\_Primary/Ethics/PRDOVR~PC-739155HS/PC-739155HS.jsp](http://www.cpa2biz.com/AST/Main/CPA2BIZ_Primary/Ethics/PRDOVR~PC-739155HS/PC-739155HS.jsp).

SEC resources are as follows:

- The SEC's January 2003 rules release is available at [www.sec.gov/rules/final/33-8183.htm](http://www.sec.gov/rules/final/33-8183.htm).

## 48

### Other Alerts

- Information for accountants, including independence, may be found online at the Office of the Chief Accountant at [www.sec.gov/about/offices/oca/ocaprof.htm](http://www.sec.gov/about/offices/oca/ocaprof.htm).
- Independence reference materials can be found on the SEC Web site at [www.sec.gov/info/accountants/independref.shtml](http://www.sec.gov/info/accountants/independref.shtml).
- U.S. Securities and Exchange Commission, Office of the Chief Accountant, 100 F Street, NE, Washington, DC 20549; (202) 551-5300 (phone); (202) 772-9252 (fax).

The PCAOB has a Web site at [www.pcaobus.org](http://www.pcaobus.org). Standards and rules can be found at [www.pcaobus.org/Standards/index.aspx](http://www.pcaobus.org/Standards/index.aspx).

GAO resources are as follows:

- Obtain the GAO Yellow Book requirements at [www.gao.gov/aac.html](http://www.gao.gov/aac.html).
- Obtain Yellow Book independence standards at [www.gao.gov/govaud/govaudhtml/d07731g-5.html#pgfId-1034319](http://www.gao.gov/govaud/govaudhtml/d07731g-5.html#pgfId-1034319).
- Obtain answers to FAQs on independence at [www.gao.gov/govaud/d02870g.pdf](http://www.gao.gov/govaud/d02870g.pdf).
- Access a slide presentation on GAO independence standards at [www.gao.gov/govaud/july2007slides.pdf](http://www.gao.gov/govaud/july2007slides.pdf).
- Direct inquiries should be sent to Michael Hrapsky, Senior Project Manager, *Government Auditing Standards*, at (202) 512-9535 or e-mail [yellowbook@gao.gov](mailto:yellowbook@gao.gov).

DOL resources are as follows:

- DOL Regulation 2509.75-9, *Interpretive bulletin relating to guidelines on independence of accountant retained by Employee Benefit Plan*. This regulation can be found at [www.dol.gov/dol/allcfr/EBSA/Title\\_29/Part\\_2509/29CFR2509.75-9.htm](http://www.dol.gov/dol/allcfr/EBSA/Title_29/Part_2509/29CFR2509.75-9.htm).
- Direct inquiries to the DOL at 1-866 4-USA-DOL.

Banking regulators' resources are as follows:

- Obtain the FDIC regulations (12 U.S. *Code of Federal Regulations* Part 363), *Annual Independent Audits and Reporting Requirements*, at [www.fdic.gov/regulations/laws/rules/2000-8500.html#2000part363](http://www.fdic.gov/regulations/laws/rules/2000-8500.html#2000part363)
- The following organizations comprise the Federal Financial Institutions Examination Council (FFIEC): Office of Thrift Supervision, Treasury; Board of Governors of the Federal Reserve System; FDIC; National Credit Union Administration; and Office of the Comptroller of the Currency, Treasury. The FFIEC issues financial institution letters (FILs), which are addressed to the CEOs of the financial institutions on the FIL's distribution list—generally, FDIC-supervised institutions. FILs may announce new regulations and policies, new FDIC publications, and a variety of other matters of principal interest to those responsible for operating a bank or savings association. FILs have addressed auditor conduct (for example, internal audit outsourcing and use of indemnification clauses in engagement letters) in recent years and may apply to both public and nonpublic institutions. See [http://search.fdic.gov/search?access=p&output=xml\\_no\\_dtd&sort=date:D:L:d1](http://search.fdic.gov/search?access=p&output=xml_no_dtd&sort=date:D:L:d1)

## Independence and Ethics Developments—2009

49

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203&filter=p for additional information.

International Federation of Accountants (IFAC) resources are as follows:

- Information about the International Ethics Standards Board for Accountants (IESBA) can be found on the IFAC's Web site at [www.ifac.org/Ethics/](http://www.ifac.org/Ethics/).
- The IESBA's *Code of Ethics for Professional Accountants* can be found at [www.ifac.org/Members/Pubs-Details.tmpl?PubID=10456070402914590&Category=Ethics](http://www.ifac.org/Members/Pubs-Details.tmpl?PubID=10456070402914590&Category=Ethics).

